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IN THE

# Supreme Court of the United States

OCTOBER TERM, 1936

No. [redacted] 3

FRED L. FOX, Individually and as State Tax Commissioner of the State of West Virginia, Appellant,

v.

THE DRAVO CONTRACTING COMPANY.

Appeal from the District Court of the United States for the Southern District of West Virginia.

## BRIEF FOR APPELLEE.

WILLIAM S. MOORHEAD,
LAWRENCE D. BLAIR,
W. CHAPMAN REVERCOMB,
W. ELLIOTT NEFFLEN,
*Counsel for the Appellee, The Dravo Contracting Company.*

SMITH BROS. CO. INC., LAW PRINTERS, 208-212 GRANT STREET, PITTSBURGH, PA.

## SUBJECT INDEX.


| | PAGE |
|---|---|
| Opinion of the Lower Court | 1 |
| Jurisdiction of the Lower Court and Supreme Court | 1 |
| Statement of Questions Involved | 2 |
| Statutes and Constitutional Provisions Involved | 3 |
| Concise Statement of the Case | 4 |
| Summary of Argument | 8 |
| Argument | 11 |
| I. The Tax Involved Is a Direct Burden Upon the Exercise of a Governmental Function and Is Unconstitutional | 11 |
| Nature of Tax | 14 |
| Cases cited by Appellant Distinguished | 16 |
| The Tax is a Direct and Immediate Burden on the Contracts of the Government | 19 |
| The Function Exercised in the Construction of the Locks and Dams was Governmental | 21 |
| The Tax is Unconstitutional | 24 |
| Cases cited by Appellant Distinguished | 29 |
| Appellee's right to Assert the Immunity Claimed | 33 |
| II. The Tax Is Assessed in Part on Gross Income of a Foreign Corporation from Transactions Entirely Outside West Virginia and Therefore Violates the Due Process Clause of the Constitution | 38 |

PAGE

III. The Tax Is Assessed in Part on Gross Income of a Foreign Corporation from Transactions in Interstate Commerce and Therefore Violates the Interstate Commerce Clause of the Constitution ..... 38

Cases Cited by Appellant Distinguished.. 39

State May not Tax Extrastate and Interstate Transactions of a Unitary Business. 41

Extrastate Transactions Involved..... 46

Interstate Transactions Involved..... 49

Extent of Extrastate and Interstate Transactions ..... 52

The Tax is Imposed upon Receipts from such Transactions ..... 55

Replacements and Improvements in Canalization of Navigable Rivers Constitute Work in Interstate Commerce 57

The Tax in this Case Cannot be Apportioned ..... 59

IV. The Tax Is Assessed in Substantial Part on Work Done on Property Over Which the United States Had Exclusive Legislative Jurisdiction ..... 62

Conclusion ..... 69

Appendix ..... 71

West Virginia Code 1931, Chap. 1, Art. 1, Secs. 3 and 4..... 71

## Table of Cases.


| | PAGE |
|---|---|
| Addyston Pipe & Steel Co. v. U. S., 175 U. S. 211 | 51 |
| Alward v. Johnson, 282 U. S. 509 | 17 |
| Ashwander v. Tennessee Valley Authority, 297 U. S. 288 | 64 |
| Baltimore Shipbuilding Co. v. Baltimore, 195 U. S. 375 | 17 |
| Battle v. United States, 209 U. S. 36 | 64 |
| Bowman v. Continental Oil Co., 256 U. S. 642 | 60 |
| Browning v. Waycross, 233 U. S. 16 | 17, 40, 41 |
| Choctaw, O. & G. R. Co. v. Harrison, 235 U. S. 292 | 20, 34 |
| Collector v. Day, 11 Wall. 113 | 34 |
| Commonwealth v. P. Lorillard Co., 129 Va. 74, 105 S. E. 683 | 60 |
| Cooney v. Mountain States Telephone & Telegraph Co., 294 U. S. 384 | 16, 56 |
| Crew Levick Co. v. Pennsylvania, 245 U. S. 292 | 20, 38, 42, 59 |
| Cudahy Packing Co. v. Minnesota, 246 U. S. 450 | 39 |
| Dahnke-Walker Milling Co. v. Bondurant, 257 U. S. 282 | 51 |
| Dobbins v. Erie County, 16 Pet. 435 | 34 |
| Dravo Contracting Company v. Fox, Tax Commissioner, 16 Fed. Supp. 527 | 1 |
| East Ohio Gas Co. v. Tax Commission, 283 U. S. 465. | 39 |
| Fargo v. Michigan, 121 U. S. 230 | 38 |
| Fort Leavenworth R. R. Co. v. Lowe, 114 U. S. 525 | 68 |
| Galveston, H. & S. A. Ry. Co. v. Texas, 210 U S. 217. | 38 |
| General Construction Company v. Fisher, et al., 149 Or. 84, 39 P. (2d) 358, appeal dismissed, 295 U. S. 715 | 18, 19, 36 |

PAGE

Union Pacific Railroad Co. v. Peniston, 18 Wall. 5 . . . . . 17, 24, 32

United States v. Ansonia Brass & C. Co., 218 U. S. 452 . . . . . 47

United States v. Arizona, 295 U. S. 174 . . . . . 23

United States v. Tucker, 122 Federal Reporter 518. 63

United States Glue Company v. Oak Creek, 247 U. S. 321 . . . . . 19, 42

Western Gas Construction Co. v. Commonwealth (affirmed in Memorandum Opinion, 276 U. S. 597) 147 Va. 235, 136 S. E. 646 . . . . . 16, 40

Western Union Telegraph Co. v. Ratterman, 127 U. S. 411 . . . . . 60

Weston v. City Council of Charleston, 2 Pet. 449 . . . 24, 34

Wiloil Corporation v. Pennsylvania, 294 U. S. 169 . . 17, 43

York Manufacturing Co. v. Colley, 247 U. S. 21 . . . . . 41

**Table of Statutes and Constitutional Provisions.**

United States Judicial Code, Sec. 266 (U. S. C. A., Title 28, Sec. 380) . . . . . 2

West Virginia Gross Sales and Income Tax Law, West Virginia Code of 1931, Chapter 11, Article 13, as amended May 26, 1933: . . . . . 3

Section 1 . . . . . 56

Section 2 (e) . . . . . 14

Section 10 . . . . . 14

West Virginia Law dealing with acquisition of lands by the United States, West Virginia Code 1931, Chapter 1, Article 1, Sections 3 and 4 . . . . . 3, 63, 71

*Table of Statutes and Constitutional Provisions.*


PAGE

Constitution of the United States:

Fourteenth Amendment..... 3

Article 1, Section 8, Clause 3, Interstate Commerce Clause..... 3

Article 1, Section 8, Clause 17, dealing with the exclusive legislative power of Congress... .....3, 63, 64, 65

IN THE

# Supreme Court of the United States

**OCTOBER TERM, 1936**

**No. 625**

FRED L. FOX, Individually and as State Tax Commissioner of the State of West Virginia, Appellant,

v.

THE DRAVO CONTRACTING COMPANY.

Appeal from the District Court of the United States for the Southern District of West Virginia.

## BRIEF FOR APPELLEE.

### OPINION OF THE DISTRICT COURT.

This case is reported in 16 Federal Supplement 527, where it is entitled *Dravo Contracting Company v. Fox, Tax Commissioner*. The findings and opinion of the District Court are printed in the Record at pages 406 to 414.

### JURISDICTION OF THE DISTRICT COURT AND THE SUPREME COURT.

This suit was instituted by a bill in equity to restrain the enforcement and execution of the Gross Sales and Income Tax Law of West Virginia by restraining the State Tax Commissioner in the enforcement or execution of that statute. It was heard and determined by a Circuit Judge and two District Judges convened in

pursuance of Section 266 of the Judicial Code (United States Code Annotated, Title 28, § 380).

A temporary restraining order had been issued pending the hearing (R. 313), and it was agreed by both parties that the hearing before the District Court should be the final hearing by that Court (R. 410).

Based on Findings of Fact and Conclusions of Law, the District Court found that it had jurisdiction as a Federal Court and as a Court of Equity (R. 409, 410). That finding is not contested.

On October 1, 1936, the District Court filed its Findings of Fact, Conclusions of Law, and Opinion, concurred in by the three Judges, and on October 24, 1936, entered the decree prayed for in the bill of complaint and enjoined the collection of the tax complained of (R. 415).

From this final decree, the defendant took an appeal to this Court under Section 266 of the Judicial Code (R. 416).

## QUESTIONS INVOLVED.

1. Is a gross income tax, assessed by a State against the receipts of a contractor under contracts entered into with the United States for the furnishing of materials and labor for the construction of locks and dams in a navigable stream, a direct burden on, and impediment to, the exercise of a governmental function?

*Answered in the affirmative by the District Court* (R. 413).

2. Is such State tax a direct burden on the extra-state and interstate transactions of the contractor, a corporation of a sister State, under such contracts and, therefore, violative of the due process clause and the interstate commerce clause of the Constitution of the United States?

*Not discussed by the District Court.*

3. If such tax is assessed indiscriminately against receipts from extrastate and interstate business and receipts from intrastate business, will the Court attempt to allocate the tax and sustain that portion thereof which it would so allocate to local business?

*Not discussed by the District Court.*

4. Where a substantial amount of the materials delivered and work done, within the geographical boundaries of a State, were delivered and done on property owned by the United States and over which it had exclusive legislative jurisdiction, can the State tax the gross receipts of the contractor for such materials and work?

*Not discussed by the District Court.*

## THE STATUTES OF WEST VIRGINIA AND PROVISIONS OF THE UNITED STATES CONSTITUTION INVOLVED.

The West Virginia Gross Sales and Income Tax Law (Chapter 11, Article 13, West Virginia Code of 1931, as amended May 26, 1933); particularly, Section 1, Section 2 (e) and Section 10 (R. 36).

West Virginia Code 1931, Chapter 1, Article 1, Sections 3 and 4, giving the consent of the State to acquisition of lands by the United States (Appendix to this Brief, p. 71).

Constitution of the United States:

Fourteenth Amendment (Due Process Clause);

Article 1, Section 8, Clause 3, (Interstate Commerce Clause);

Article 1, Section 8, Clause 17, (Exclusive Legislative jurisdiction over land purchased by the United States with the consent of the State).

## CONCISE STATEMENT OF THE CASE.

This suit involves a proceeding in equity to enjoin the collection of the West Virginia Gross Sales and Income Tax in respect of receipts by plaintiff below from four contracts with the United States for the erection of locks and roller gate dams on the Kanawha and Ohio Rivers.

After the filing of bill of complaint and answer, plaintiff below and defendant below entered into a Stipulation of Facts (R. 338).

Although the plaintiff below based its prayer for relief on several distinct positions, the District Court rested its decree on one conclusion, namely, that, in the construction of the locks and roller gate dams covered by the four contracts, the United States was engaged in the exercise of a proper governmental function for the improvement of navigable rivers and that the imposition of the Gross Sales and Income Tax was a direct burden thereon which the State of West Virginia had no power to impose (R. 410).

After final hearing, the District Court filed its Findings of Fact, Conclusions of Law, and Opinion, concurred in by the three Judges, entered the decree prayed for, and enjoined the collection of the tax assessed against the gross receipts of the plaintiff from the four Government contracts referred to (R. 406-414).

The Court below found that there was no dispute as to the facts, in as much as they were stipulated (R. 406). The Court set forth, however, specifically certain facts shown by the Stipulation which it regarded as material to its decision (R. 406).

Appellant's Statement of the Case is inaccurate in the assertion that appellee contends that it is an agent

or instrumentality of the United States (Appellant's Brief, pp. 5 and 6). The appellee's position on that point is stated at page 11 hereof.

The said Statement is also inaccurate in respect of some of the asserted conclusions of the District Court. We have stated above the conclusion upon which the decree of the Court below was based.

The said Statement omits the following facts, which we regard pertinent in considering this appeal, amplifications of which will appear in the argument:

In pursuance of reports and recommendations of the Secretary of War, Congress enacted legislation and made appropriations for a deeper and wider channel in the Kanawha River in West Virginia (R. 98). This was to be done by constructing four locks and dams to replace thirteen existing ones, ten of which were on the Kanawha and three on the Ohio River (R. 271, 272, 340).

The sites were located and land was acquired by the United States on both sides of the river at the respective sites, with the consent of West Virginia (R. 381, Appendix hereto p. 71).

Specifications were prepared and notices and invitations for bids were given to appellee, among others. The four jobs were awarded to appellee on its respective bids and four separate contracts, one for the locks and dam at each site, were entered into between the United States and the appellee, a Pennsylvania corporation, whose office and only shops and factories are located at Neville Island, Pittsburgh, Pa. (R. 342, 346)

These contracts were for the furnishing of all labor, materials, and work for the construction of the respective locks and dams (London Contract, R. 61, which is

similar to other contracts, except as noted, R. 427, 430, 434).

The consideration to be paid was not a lump sum, but a sum based on designations and unit rates specified in schedules appended to the contracts. For certain units of machinery, fixed sums were nominated (R. 62).

The statute assessing the gross sales and income tax, involved in this case, was passed on May 26, 1933 (R. 26), when that tax was increased from 3/10 of 1% to 2% (R. 384). Two of the contracts in suit were made before the statute was amended (R. 341). Appellee's estimated costs and bids on the four contracts did not include any items to cover the gross income tax (R. 375). In its estimates for the London and Marmet jobs, no percentage was added for profit. In the Winfield job, 5% was added, and in the Gallipolis contract, 6% was added for profit (R. 375).

The dams are not the usual concrete emplacements, but are of a comparatively new type, so designed as to raise or lower the height of the water in the pools (R. 354). This is accomplished by huge cylindrical gates, each weighing about 225 tons, which can be raised or lowered electrically on rachets or racks (R. 352, 353). As part of this mechanism and for other purposes, such as the operation of a crane and service cab, a large structural steel service bridge is superimposed on the dam (R. 352, 353). There is a power house on the dam equipped with machinery to operate each roller gate and the lock gates (R. 98).

A glance at the photographs of the locks, dams, machinery, and equipment, which are a part of the Record, will portray this better than our words.

Appellee purchased all of the materials for the roller gates, lock gates, cranes, racks, spur rims, structural

steel, patterns, hoisting mechanism and equipment outside West Virginia and, as specified in the bids and contracts, fabricated them at its shops at Neville Island, Pennsylvania (R. 350).

After fabrication, this machinery and equipment was inspected by the Government (R. 350), paid for in part (R. 344), title thereto taken by the Government (R. 68), and stored at Neville Island awaiting shipment (R. 351).

At appropriate times, this machinery and equipment belonging to the United States was then disassembled into suitable units and transported by river craft and barges down the Ohio and up the Kanawha to the respective sites (R. 351). The roller gates, hoisting apparatus, lock gates, and equipment were then unloaded from the barges onto the dams and piers and into positions prepared for them (R. 351, 353).

Materials purchased by appellee outside West Virginia were transported to the dam sites and unloaded from barges and installed in the locks and dams (R. 356). Some of the materials so shipped were stored temporarily on Government property at the work sites (R. 356).

Appellee purchased some material, such as lumber, bolts, cable, sand, gravel, reinforcing steel, riprap, and forms for coffer dams in West Virginia, which was delivered by the seller on Government land and installed in the dams (R. 356).

Other details of these operations appear in the Stipulation (R. 349-357).

Appellee owned or leased a large flotilla of river craft which it used in the construction of the locks and dams, such as barges, dredges, derrick boats, whirlers,

and towboats. All this river craft was taken from Pennsylvania by river into West Virginia and brought back in so far as not required on the jobs not yet completed (R. 356, 357).

Payments under the contracts were made monthly or semi-monthly by checks mailed to the appellee at Pittsburgh (R. 344).

The payments were based on estimates made by representatives of the Government for—

1. Materials delivered to the appellee at its Neville Island Shops, Pittsburgh;

2. Materials fabricated by the appellee at its Neville Island Shops, Pittsburgh;

3. Materials delivered, including fabricated materials, at the dam site;

4. Work done at the dam sites.

A retained percentage of 10% on each estimate was paid upon final acceptance of the completed work (R. 345).

## SUMMARY OF ARGUMENT.

### I.

The tax in suit is a gross income tax and differs substantially from limited foreign corporation license taxes and property taxes. Appellee, a corporation of Pennsylvania, paid such license and property taxes to West Virginia. The tax in suit is in addition to those taxes.

The tax in suit differs from a net income tax.

License, property, and net income taxes are, or may be, incidental and remote. A gross income tax is an

immediate and direct burden on the business whence the income arises.

The income taxed in this case came from four contracts between the United States and the appellee for the construction of locks, dams, and equipment in a navigable river. These contracts were the means or method adopted by the United States in the exercise of a governmental function.

The tax in suit is a direct burden on the performance of that constitutional function. The tax is, therefore, unconstitutional and invalid.

Appellee has a right to assert the immunity of the contracts from the tax in question.

This proposition was sustained by the District Court.

II. and III.

The tax is imposed on receipts from transactions entirely outside West Virginia and, therefore, violates the due process clause of the Constitution.

It is also imposed on receipts from transactions in interstate commerce and, therefore, violates the interstate commerce clause of the Constitution.

These propositions were not discussed in the opinion of the District Court, but were argued below and are contested under heading I of appellant's brief at page 20.

A gross income tax is a direct burden on the business affected. If it is imposed by a State against the receipts of a foreign corporation from essentially extrastate and interstate transactions, it is unconstitutional and unenforceable; even though it might have been valid, if such receipts had been segregated from

receipts from local business and the tax imposed only on the latter. If such segregation is not made in the assessment, the courts will not make it and the entire assessment falls.

An analysis of the contracts shows many severable transactions entirely extrastate and interstate in character. Such transactions were contemplated and, in many cases, required by the contracts.

The erection of locks and dams to replace existing ones on a navigable river, used by vessels during the replacement work, is itself work in interstate commerce.

## IV.

A substantial part of the work done and materials delivered was on land purchased by the United States with the consent of West Virginia on both sides of the river at the dam sites. Over this land the Congress had exclusive legislative jurisdiction. West Virginia is without power to tax operations thereon. If the receipts from such operations are not excluded from the assessment, it must fall in its entirety; for the Courts will not make the separation, if the statute and the Tax Commissioner did not.

This proposition becomes material only if proposition I, II, or III is not sustained. It was not discussed in the opinion of the District Court, but was argued at the hearing, and is dealt with under heading III of appellant's brief at page 33.

## ARGUMENT

The argument in appellant's brief is made under six headings. We have not followed that arrangement; because we think that the first proposition to be discussed should be the conclusion upon which the District Court rested its decision, rather than the interstate and extrastate commerce aspect of the case, which is argued under appellant's proposition I and our propositions II and III.

The decision of the court below is attacked under propositions II, V, and VI of appellant's brief and is dealt with under proposition I of our brief.

### I.

### The Tax Involved Is a Direct Burden Upon the Exercise of a Governmental Function and Is, Therefore, Unconstitutional

This proposition was argued by counsel for appellee in the District Court and was distinctly affirmed in the Conclusions of Law and the Opinion (R. 410, 413).

Counsel for appellant ascribe to appellee a substantially different proposition, and then proceed to attack it. At page 5 of appellant's brief, it is stated that appellee contends that "it is an instrumentality of the United States", and at page 6, that "it was an agent or instrumentality of the United States". That appellee is an independent contractor and not an instrumentality of the Government is argued under heading II at page 28 of appellant's brief.

We have not contended and do not contend that appellee is or was an agent or instrumentality of the

United States. It is not, and is not pretended to be, a governmental agency or instrumentality such as, for instance, the various "Authorities" which have been created in the last few years, the Reconstruction Finance Corporation, or the Emergency Fleet Corporation. Dravo Contracting Company is an independent contractor.

We do assert, however, that the four contracts entered into by the Government with the Dravo Contracting Company were the means, or instrumentalities, if you like, by which the United States performed a governmental function in improving the navigability of the Great Kanawha River through the construction of locks and roller gate dams.

There is no inherent attribute of the Dravo Company which renders it exempt from the tax sought to be imposed; but the governmental contracts are exempt from the direct burden imposed by the tax. In other words, the Gross Sales and Income Tax is a burden upon, and an impediment to, the performance of a governmental function and the means or method adopted by the Government to perform that function. The burden is direct and immediate, because the tax is imposed on every dollar received by the Dravo Company from the Government under the contracts.

It is argued by appellant in his brief under heading V at page 45, in effect, that a privilege tax on the gross receipts of a contractor under a contract with the United States does not constitute a direct burden upon its operations. Before discussing the law, let us see just how a gross receipts tax imposed by a State, if enforceable, affects the United States in the exercise of a constitutional power.

If the tax in suit is what it purports to be—a privilege tax—, the exercise of the privilege is conditioned on the payment of the tax. No one can do business with the United States unless he pays tribute to the State. If the tax exacts a percentage of the gross receipts, it diverts moneys intended for material and services to the coffers of the State. If the tax is included in the bid of the contractor, the cost to the Government of the materials and work is increased. If the tax is not included, the financial ability of the contractor to carry out the contract is impaired or, conceivably, ruined, and the performance of the contract is impeded or, possibly, prevented. Whether the tax is included or not, the free exercise of a power is impaired. Peradventure the tax may be imposed after the contract is let. If the bid is at or near cost and the rate of the tax is high, the performance of the contract may actually be rendered impossible.

The tax could be at a rate which would actually prevent the United States from doing its work by contract. It may be said that it could do the work directly by its own employees and thus escape the tax, but, if it were forced so to do, the tax would be an impediment to the choice of means by the United States, which a state cannot impose.

The appellee in the case at bar, however, did not include in its estimated costs or bids on any of the four contracts any item to cover the West Virginia Gross Sales and Income Tax. This is an admitted fact (R. 375). At the time the London and Marmet contracts were entered into, the gross income tax was at the rate of 3/10 of 1%, but was subsequently increased to 2% (R. 343, 384). Furthermore, in its estimates for the London and Marmet jobs, appellee added no percentage

for profit (R. 375), business in the year 1932 being slack and appellee desiring to provide work for its employees. The bids on the Winfield and Gallipolis jobs included estimated items of 5% and 6%, respectively, for profit.

While the appellee did not consider the tax in suit applicable to its receipts from the Government contracts in suit, if the assessment involved is upheld, the appellee and any future bidders on a government contract will necessarily be obliged to add the amount of the tax to their bids.

## THE NATURE OF THE TAX

The law imposing the tax is entitled "The Gross Sales and Income Tax Law" (R. 26).

Section 2 (R. 28) levies "annual privilege taxes against the persons, on account of the business and other activities, and in the amounts to be determined by the application of rates against values or gross income, as follows:

"* * *

"(e) Upon every person engaging or continuing within this state in the business of contracting, the tax shall be equal to two per cent of the gross income of the business;" (R. 30)

Section 10 provides,

"Sec. 10. The tax imposed by this article shall be in addition to all other licenses and taxes levied by law as a condition precedent to engaging in any business, trade or calling. A person exercising a privilege taxable under this article, subject to the payment of all licenses and charges which are condition precedent to exercising the privilege taxed,

may exercise the privilege for the current tax year upon the condition that he shall pay the tax accruing under this article." (R. 36)

The tax involved in this case is, therefore, a privilege tax levied on the gross income of the business of contracting and is *in addition* to all other licenses and taxes.

The tax in question is not indirect or incidental.

It is not a tax on property. The appellee paid the *ad valorem* property taxes assessed against its personal property by the State of West Virginia and its political subdivisions for the years in question in the aggregate amount of $5,790.62 (R. 385).

It is not a license tax on foreign corporations doing business in West Virginia. The appellee, a Pennsylvania corporation, paid such license taxes for the years in question (R. 345, 346).

The tax, the validity of which is contested, is not that portion of the Gross Sales and Income Tax assessed against local work done by the appellee in West Virginia for persons other than the United States Government. During the years in question, the appellee performed such work, made returns of its gross income therefrom, and paid the Gross Sales and Income Tax thereon (R. 384).

The tax involved in this case is in addition to all those taxes (R. 345).

The tax contested in this case is a tax on the privilege of doing business with the United States. It is a direct tax on that business. It is assessed against every

dollar received by the appellee from the Government under the contracts in question.

It is a different kind of tax from the taxes dealt with in the cases relied on by appellant. Those cases may be classified and distinguished, as follows:

FOREIGN CORPORATION LIMITED LICENSE TAX

*Kansas City Structural Steel Co. v. Arkansas,* 269 U. S. 148.
($1,000 fine for not registering as foreign corporation).

*General Railways Signal Co. v. Virginia,* 246 U. S. 500.
($1,000 limited license fee).

*Ralph Sollitt & Sons Construction Company v. Commonwealth,* 161 Va. 854, 172 S. E. 290 (appeal dismissed for want of a substantial federal question, 292 U. S. 599.
($250 limited license fee, characterized as "a mere bagatelle").

*Western Gas Construction Company v. Commonwealth,* 147 Va. 235, 136 S. E. 646.
(Fine for not obtaining a license).

A license tax is imposed on a foreign corporation if it does any business in the State, however little. If limited in amount it is sustained, even though the corporation also transacts interstate business. If the tax is unlimited in amount or is increased by reason of the interstate business done, it is invalid; *International Paper Company v. Massachusetts,* 246 U. S. 135; *Cooney v. Mountain States Telephone & Telegraph Company,* 294 U. S. 384.

Appellee admits it did some local business in West Virginia. It paid the Gross Sales and Income Tax thereon (R. 384) and the foreign corporation license fee imposed by that State (R. 345, 346).

OCCUPATION TAX, FLAT

*Browning v. Waycross*, 233 U. S. 16 ($25 occupation tax incident to erecting lightning rods).

PROPERTY TAX

*Baltimore Shipbuilding and Dry Dock Co. v. Baltimore*, 195 U. S. 375.

*Gromer v. Standard Dredging Co.*, 224 U. S. 362.

*Alward v. Johnson*, 282 U. S. 509. (Not cited by appellant).

(The tax involved was held to be a property tax, this Court saying (p. 514), "There was no tax upon the contract for such carriage; the burden laid upon the property employed affected operations of the Federal Government only remotely.")

*Wiloil Corporation v. Pennsylvania*, 294 U. S. 169.

(Liquid fuels after delivery are taxable like any other property within the state).

*Union Pacific Railroad Co. v. Peniston*, 18 Wall. 5.

It is admitted appellee paid the *ad valorem* property taxes assessed by West Virginia (R. 385).

DOMESTIC CORPORATION TAX

*Matson Navigation Company v. State Board of Equalization of California,* 297 U. S. 441.
*New York, ex rel. Cohn v. Graves et al.,* No. 404 October Term, 1936, decided by this Court March 1, 1937.

The case last cited relates to an individual instead of a corporation, but the same principle is involved. Neither of the last two cases is cited by appellant.

The appellee is not a corporation of West Virginia, but a corporation of Pennsylvania, where its offices and only shops are located (R. 346).

NET INCOME TAX

*General Construction Company v. Fisher et al.,* 149 Or. 84, 39 P. (2d) 358, (appeal dismissed for want of a substantial federal question, 295 U. S. 715).
*Metcalf & Eddy v. Mitchell,* 269 U. S. 514.
*Kreipke v. Commissioner of Internal Revenue,* 32 F. (2d) 594.

Counsel for appellant frankly admit that the cases cited at pages 20 to 26 of their brief "do not involve a tax of the character here involved" (appellant's brief, page 26).

At page 45 of their brief, counsel state:

"So far as the principle of interference with a function or instrumentality of the Federal Government is concerned, it is not believed that there is any distinction between a tax on net income and a tax on gross income."

But counsel admit that a gross income tax on receipts from interstate commerce is invalid (appellant's brief, 55). It is invalid because it is a direct burden on the business affected. If this be true, it necessarily follows that a gross income tax on receipts from a government contract is a burden on the business covered by the contract and cannot be imposed by a State. In the words of this Court a State "may not lay any tax *upon transactions* by which the United States secures the things desired for its governmental purposes"; *Panhandle Oil Co. v. Mississippi,* 277 U. S. 218, 221 (Italics ours).

Counsel for appellant quote at length from the cases of *General Construction Co. v. Fisher,* 149 Or. 84, 39 P. (2d) 358 (appeal dismissed for want of a substantial federal question, 295 U. S. 715), and *Metcalf & Eddy v. Mitchell,* 269 U. S. 514. The first case involved a net income tax enacted by the State of Oregon and assessed against receipts of the plaintiff from a contract with the United States in connection with the Owyhee Irrigation Project. The second case involved the federal net income tax assessed against the payments made to consulting engineers by states or subdivisions of states for services in connection with water supply and sewage disposal systems. Both of these cases involved net income taxes, which taxes we contend are indirect and incidental, whereas a gross income tax is direct and immediate.

The distinction between a gross income tax and a net income tax is clearly drawn in the opinion of this Court in the case of *United States Glue Company v. Oak Creek,* 247 U. S. 321, wherein it is said at pages 328 and 329:

> "The difference in effect between a tax measured by gross receipts and one measured by net in-

come, recognized by our decisions, is manifest and substantial, and it affords a convenient and workable basis of distinction *between a direct and immediate burden upon the business affected and a charge that is only indirect and incidental.* A tax upon gross receipts affects each transaction in proportion to its magnitude and irrespective of whether it is profitable or otherwise. Conceivably it may be sufficient to make the difference between profit and loss, or to so diminish the profit as to impede or discourage the conduct of the commerce. A tax upon the net profits has not the same deterrent effect, since it does not arise at all unless a gain is shown over and above expenses and losses, and the tax cannot be heavy unless the profits are large." (Italics ours).

A gross sales and income tax is a tax on business. In the case of *Choctaw, Oklahoma & Gulf Railroad Company v. Harrison,* 235 U. S. 292, this Court said at page 299 of its opinion:

"A tax upon a merchant's, manufacturer's, or miner's gross sales is not the same thing as one on his stock treated as property. Cooley on Taxation (3rd ed.), p. 1095. The former is upon his business."

In *Crew Levick Co. v. Pennsylvania,* 245 U. S. 292, 297, a gross income tax was characterized as follows: "It operates to lay a direct burden upon every transaction in commerce by withholding, for the use of the State, a part of every dollar received in such transactions."

A sales tax levied against the sums payable under a Government contract is a burden on the performance

of a governmental function and it is immaterial whether the seller or purchaser is required to pay the tax. *Panhandle Oil Company v. Mississippi,* 277 U. S. 218, 222.

It would appear to be perfectly clear, therefore, that the Gross Sales and Income Tax involved in this case is a direct burden on the contracts entered into by the United States with appellee. It is an immediate impediment on the privilege of doing business with the Government.

Were the contracts entered into in the exercise of a Governmental function?

**THE FUNCTION EXERCISED BY THE UNITED STATES UNDER THE CONTRACTS FOR THE CONSTRUCTION OF THE LOCKS AND DAMS**

It is stipulated that "the United States constructed said locks and dams for the development and improvement of navigation" (R. 382).

The letter of the Secretary of War to the Speaker of the House of Representatives gives the history of the development of navigation on the Kanawha River, is printed in the Record at pages 270 to 309, and is stipulated to be a true copy (R. 340).

The Kanawha River is ninety-seven miles long, is entirely within West Virginia, and enters the Ohio River at Point Pleasant, W. Va., two hundred sixty-six miles below Pittsburgh (R. 271).

Prior to 1869, expenditures had been made to improve the channel of the Kanawha. Down to 1874, moneys for the improvement of navigation had been expended by the Government and the State of West Vir-

ginia, but after that time West Virginia took no part in the improvement of the stream (R. 284 and 285). By the year 1898, the United States had expended over $4,000,000 in construction of ten locks and dams, six above Charleston, W. Va., and four below. These afforded a six foot channel (R. 271). The four locks and dams covered by the contracts in suit were built to replace the ten old locks and dams and to provide a nine foot channel (R. 271, 272). Transportation had been seriously hampered because of the lack of adequate depth and the anticipated increase in commerce was deemed sufficient to justify the cost of the improvement (R. 273).

Apparently, the Government had been beset by complaints concerning the inadequate navigation facilities on the Kanawha (R. 285). One of the desires seems to have been to ship coal up the Ohio River (R. 286). It seems that river craft used on the Ohio River could not be navigated with facility on the Kanawha on account of the difference in the depth of the channels of the two streams (R. 286).

The dams were constructed with roller gates which could be raised or lowered, so as to control the water in the pools, and were so designed that the power created by the damming of the water could be used for the generation of electricity (R. 354 and 382). Water power at two of the dams is now being used for the generation of electricity under a license granted by the United States to a private corporation, the Kanawha Valley Power Company (R. 382).

The contract between the Government and the Power Company expressly provides, however, that the latter must not do anything in the exercise of its license that will interfere with navigation (Findings of Fact, R. 408).

It is well established that the exclusive power in Congress to regulate commerce upon the navigable streams used in trade between the states includes the absolute right to place obstructions and make alterations in such rivers, designed to facilitate navigation. *South Carolina v. Georgia,* 93 U. S. 4; *United States v. Arizona,* 295 U. S. 174. In the latter case, this Court said (p. 183):

> "But the title of the State is held subject to the power granted to Congress by the commerce clause, *United States v. Holt State Bank,* 270 U. S. 49, 54-55, and under that clause Congress has power to cause to be built a dam across the river in aid of navigation."

The contention made by appellant in the lower court that the construction of the dams, so as to permit of the use of the water power thus created for the generation of electricity impinges on the character of the project as a governmental function is put to rest by the opinion of this Court in the case of *New York ex rel. Rogers v. Graves, et al.,* No. 139 October Term, 1936, in which this Court said, in an opinion delivered on January 4, 1937, by Mr. Justice Sutherland (p. 206):

> "The primary purpose of the enterprise being legitimately governmental, its incidental use for private purposes affords no ground for objection. United States v. Chandler-Dunbar Water Power Co., 229 U. S. 53, 73, 57 L. ed. 1063, 1079, 33 S. Ct. 667; Ashwander v. Tennessee Valley Authority, 297 U. S. 288, 333, 80 L. ed. 688, 703, 56 S. Ct. 466."

There appears to be no room for doubt that, in entering into the four contracts with the appellee, the War Department of the Government was acting under the authority conferred by Congress in the exercise of a

constitutional function in the improvement of navigation on a navigable river.

THE WEST VIRGINIA GROSS SALES AND INCOME TAX BEING A DIRECT BURDEN ON THE PERFORMANCE OF A GOVERNMENTAL FUNCTION IS UNCONSTITUTIONAL

There is a long line of cases which follow *McCulloch v. Maryland,* 4 Wheat. 316, 436, in holding that

> "the states have no power, by taxation or otherwise, to retard, impede, burden, or in any manner control, the operations of the constitutional laws enacted by Congress to carry into execution the powers vested in the general government."

Among those cases are *Osborn v. Bank of the United States,* 9 Wheat. 738; *Union Pacific Railroad Co. v. Peniston,* 18 Wall. 5; *Weston v. Charleston,* 2 Pet. 449; *Panhandle Oil Company v. Mississippi,* 277 U. S. 218.

In the two rather recent decisions of this Court, which we are about to consider and quote from, the line is clearly drawn between a tax imposed directly on receipts from a Government contract (which the tax in suit is), and an indirect tax on the property used or purchases made by the contractor in the performance of a Government contract (which the tax in suit is not).

In *Panhandle Oil Company v. Mississippi,* 277 U. S. 218, it appeared that Mississippi had imposed a tax on the sale of gasoline and sued to recover taxes on sales of gasoline to the United States for the operation of its Coast Guard Fleet and Veterans' Hospital. The Supreme Court of Mississippi held the tax valid, but the Supreme Court of the United States re-

versed the decision, holding the tax unconstitutional. Mr. Justice Butler, in delivering the opinion of this Court, said (pp. 221, 222):

> "The United States is empowered by the Constitution to maintain and operate the fleet and hospital. Art. 1, § 8. That authorization and laws enacted pursuant thereto are supreme (Art. 6); and, in case of conflict, they control state enactments. *The States may not burden or interfere with the exertion of national power or make it a source of revenue or take the funds raised or tax the means used for the performance of Federal functions. McCulloch v. Maryland,* 4 Wheat. 316, 425, *et seq. Dobbins v. The Commissioners of Erie County,* 16 Pet. 435, 448. *Ohio v. Thomas,* 173 U. S. 276. *Choctaw & Gulf R. R. Co. v. Harrison,* 235 U. S. 292. *Indian Oil Co. v. Oklahoma,* 240 U. S. 522. *Johnson v. Maryland,* 254 U. S. 51. *Clallam County v. United States,* 263 U. S. 341, 344. *Northwestern Mutual Life Ins. Co. v. Wisconsin,* 275 U. S. 136. *New Brunswick v. United States,* 276 U. S. 547. The strictness of that rule was emphasized in *Gillespie v. Oklahoma,* 257 U. S. 501, 505. The right of the United States to make such purchases is derived from the Constitution. The petitioner's right to make sales to the United States was not given by the State and does not depend on state laws; it results from the authority of the national government under the Constitution to choose its own means and sources of supply. While Mississippi may impose charges upon petitioner for the privilege of carrying on trade that is subject to the power of the State, *it may not lay any tax upon transactions by which the United States secures the things desired for its governmental purposes.*

"The validity of the taxes claimed is to be determined by the practical effect of enforcement in respect of sales to the government. *Wagner v. City of Covington,* 251 U. S. 95, 102. A charge at the prescribed rate is made on account of every gallon acquired by the United States. *It is immaterial that the seller and not the purchaser is required to report and make payment to the State.* Sale and purchase constitute a transaction by which the tax is measured and on which the burden rests. The amount of money claimed by the State rises and falls precisely as does the quantity of gasoline so secured by the Government. It depends immediately upon the number of gallons. The necessary operation of these enactments when so construed is directly to retard, impede and burden the exertion by the United States of its constitutional powers to operate the fleet and hospital. *McCulloch v. Maryland, supra,* 436. *Gillespie v. Oklahoma, supra,* 505. *Jaybird Mining Co. v. Weir,* 271 U. S. 609, 613. To use the number of gallons sold the United States as a measure of the privilege tax is in substance and legal effect to tax the sale. *Telegraph Co. v. Texas,* 105 U. S. 460. *Frick v. Pennsylvania,* 268 U. S. 473, 494. And that is to tax the United States—to exact tribute of its transactions and apply the same to the support of the State.

"The exactions demanded from petitioner infringe its right to have the constitutional independence of the United States in respect of such purchases remain untrammeled. *Osborn v. United States Bank,* 9 Wheat. 738, 867. *Telegraph Co. v. Texas, supra.* Cf. *Terrace v. Thompson,* 263 U. S. 197, 216." (Italics ours).

It is submitted that there is no distinction between a tax of specified cents per gallon on gasoline sold to the United States and a tax of a per cent of the gross receipts for materials and machinery delivered to, and work done for, the United States, in so far as the direct burden of those taxes on the respective transactions is concerned. If one of those taxes is unconstitutional, the other is also.

We do not contend that, if a sales tax was imposed on purchases made by the appellee of material that went into the construction of the dam or on gasoline which it used for the operation of its shovels or derricks, the appellee would be exempt from such taxes. They would be incidental and remote. Many such taxes were probably paid by the appellee.

In *Trinityfarm Construction Co. v. Grosjean*, 291 U. S. 466, it appeared that the Construction Company had contracts with the United States for the construction of levees in Louisiana for the control of the waters of the Mississippi River. In this work the contractor purchased and used gasoline. The state sought to collect a tax of 5¢ per gallon on the gasoline so purchased. The Supreme Court sustained the validity of the tax on the ground that it was not a tax on the contract for constructing the levee, but was in the nature of *a tax imposed upon the property of the contractor*. This Court said (pp. 471, 472):

> "The power granted by the commerce clause is undoubtedly broad enough to include construction and maintenance of levees in aid of navigation of the Mississippi River, and to authorize the performance of the work directly by government officers and employees or pursuant to contracts such as those awarded to appellant. The latter method

was chosen and the validity of the challenged tax is to be tested on that basis. *It is not laid upon the choice of means, the making of the contracts, the contracts themselves, or any transaction to which the federal government is a party or in which it is immediately or directly concerned. Nor is the exaction laid or dependent upon the amounts, gross or net, received by the contractor.* The exaction in respect of its relation to the federal undertaking is wholly unlike those considered in *Choctaw, O. & G. R. Co. v. Harrison,* 235 U. S. 292; *Indian Oil Co. v. Oklahoma,* 240 U. S. 522; and *Gillespie v. Oklahoma,* 257 U. S. 501. Appellant is an independent contractor. *Casement v. Brown,* 148 U. S. 615, 622. It is not a government instrumentality. Cf. *Metcalf & Eddy v. Mitchell,* 269 U. S. 514. *Group No. 1 Oil Corp. v. Bass,* 283 U. S. 279. Unquestionably, as appellant here concedes, Louisiana is free to tax the machinery, storage tanks, tools, etc., that are used for the performance of the contracts. These things are as closely connected with the work as is the gasoline in respect of which is laid the excise in question. There is no room for any distinction between the plant so employed and the gasoline used to generate power. If the payment of state taxes imposed on the property and operations of appellant affects the federal government at all, it at most gives rise to a burden which is consequential and remote and not to one that is necessary, immediate or direct. *Thomas v. Gay,* 169 U. S. 264, 275. *Metcalf & Eddy v. Mitchell, supra,* 524, *et seq. Wheeler Lumber Co. v. United States,* 281 U. S. 572, 579. Appellant's claim of immunity is without foundation." (Italics ours).

In the case at bar, the tax is "laid upon the choice of means, * * * the contracts themselves", and upon a "transaction to which the federal government is a party or in which it is immediately or directly concerned." Furthermore, the exaction is "laid or dependent upon the amounts, gross or net, received by the contractor."

The decision of the District Court in *Silas Mason Co. v. Henneford, et al.*, 15 Federal Supplement 958, cited by appellants at page 31 of their brief, involved two points.

The first was whether a tax on the privilege of using personal property in the State of Washington based upon the purchase price of such property, with certain deductions, could be imposed on material purchased by the plaintiff and used by it in construction work under a contract with the United States. The effect of the tax on the contract with the United States was just as incidental and remote as the tax involved in the *Trinityfarm Construction Company case.* The tax was not on receipts for materials delivered to, or work done for, the United States, such as the tax involved in the *Panhandle Oil Company case* and the case at bar. The District Court held that the tax was not objectionable on this point.

The second point involved the question as to whether the tax was discriminatory against interstate commerce. The District Court held that it was; but that decision was reversed by this Court in an opinion delivered by Mr. Justice Cardozo on March 29, 1937 (No. 418). That opinion did not discuss the first point.

At pages 49 to 53 of his brief, appellant quotes at length from the case of *Silas Mason Co., Inc. v. State*

*Tax Commission,* 61 P. (2d) 1269, and refer to *Ryan v. State,* 61 P. (2d) 1276, as its companion.

These two cases were argued before the Supreme Court of Washington "on the same day, upon records containing identical statements of facts" (p. 1279). Both cases involved contracts with the United States for work on the Columbia Basin Project. This Project was one in which the United States and the State of Washington cooperated and was a huge undertaking, the object of which was to promote navigation, develop power for industrial purposes, and provide for irrigation and flood control. As the Supreme Court of Washington said, at page 1283,

> "The Federal government at present furnishes the money, supervises the work, and will, for a time, maintain the operation of the project. The state, on the other hand, has furnished a large amount of money for the preliminary work and now, through the Columbia Basin Commission [a state commission], acts in an advisory capacity to the federal government in the further progress of the work. The state also has an option to take over the entire project when completed. The federal government is involved in a huge undertaking, the object of which is to promote navigation, develop power, and provide for irrigation. The state is likewise concerned."

At page 1282 of its opinion, the Court said:

> "But irrigation, flood control, and power development (except in so far as the latter two are intended to promote navigation or else some war measure or the national defense), while they may be of national interest and serve a public purpose, are not functions enjoined upon the federal govern-

ment by the Constitution, nor are they delegated to the United States by the Constitution, nor is it necessary that they be committed, for their operation, to the exclusive jurisdiction of the United States government. Legislative power, with reference to such things, is reserved in the state."

It, therefore, appears that this Project was a joint enterprise by the United States and the State of Washington. Irrigation, power development, and flood control were not incidental purposes, but primary purposes. If the State exercises its option, it will own the entire Project.

It may well be doubted that this joint project is an exercise of a strictly governmental function by the United States which a State cannot burden by taxation. It is fundamentally different from the construction of the locks and dams in the case at bar, solely by the United States admittedly in the exercise of a governmental function.

In addition to this, these cases were apparently argued on the theory that the contractors were strictly governmental agencies and, when the Court arrived at the correct conclusion that they were not, their gross receipts from the government were held subject to the tax. No consideration was apparently given to the fact that the tax might have been a burden on a governmental function and invalid for that reason, though not invalid on account of any inherent governmental attribute of the contractors.

Appeals from these cases (Nos. 773 and 774) have been taken to this Court and probable jurisdiction has been noted.

We are not here concerned with the nature of the contractor, but with the effect of the tax. This distinction is drawn in the case of *Union Pacific Railroad Company v. Peniston,* 18 Wall. 5, 36, as follows:

> "It is, therefore, manifest that exemption of Federal agencies from State taxation is dependent, not upon the nature of the agents, or upon the mode of their constitution, or upon the fact that they are agents, but upon the effect of the tax; that is, upon the question of whether the tax does in truth deprive them of power to serve the government as they were intended to serve it, or does hinder the efficient exercise of their power. A tax upon their property has no such necessary effect. It leaves them free to discharge the duties they have undertaken to perform. *A tax upon their operations is a direct obstruction to the exercise of Federal powers.*" (Italics ours)

Our contention is *not* that the Dravo Contracting Company is a governmental agency and, as such, exempt from state taxation.

Our contention is that the contracts for the erection of the locks and dams were the means employed by the Government in carrying out a governmental function and that those contracts are exempt from a State gross income tax. Such a tax, as we have seen, is a direct and immediate burden on the business covered by the contracts. If the contracts are Government contracts, the gross income tax is a burden on, and interference with, the Government in the exercise of its powers.

It is submitted that the District Court was correct in its conclusion

"That the imposition of the tax here involved constitutes a direct burden upon a lawful and proper project of the United States Government and that the State of West Virginia has no power to impose upon and collect from the plaintiff this tax." (R. 410)

**APPELLEE HAS THE RIGHT TO RESTRAIN THE COLLECTION OF THE TAX ON THE GROUND THAT IT IS UNCONSTITUTIONAL**

At page 56 of appellant's brief it is argued that "appellee has no right to complain of the tax imposed in this case, the federal government not complaining nor having commissioned appellee to intervene in its behalf." Appellee's right to make the complaint was not questioned in the Answer.

As we understand appellant's contention, it relates solely to the right of appellee to contest the tax on the ground that it impedes or burdens the United States in the exercise of a governmental power.

To sustain appellant's position, it will be necessary to overrule a long line of decisions in which this Court has held certain taxes imposed by states to be unconstitutional, on the ground that they impeded the exercise of federal powers, at the suit of the private party against whom the tax was assessed.

The following cases are a few, of many that might be cited, in which an individual or a corporation was permitted to recover back, or resist the imposition of, taxes imposed by states, on the ground that such taxes interfered with or burdened the Government in the exercise of constitutional powers:

*Dobbins v. Erie County,* 16 Pet. 435;
*Choctaw, O. & G. R. Co. v. Harrison,* 235 U. S. 292;
*New York ex rel. Rogers v. Graves* (U. S. Supreme Court), No. 139 October Term, 1936, decided January 4, 1937;
*Weston v. City Council of Charleston,* 2 Pet. 449;
*Panhandle Oil Company v. Mississippi,* 277 U. S. 218.

The following will serve as examples of many cases in which an individual or a corporation was permitted to recover back, or resist the collection of, certain federal taxes, on the ground that they interfered with or impeded the exercise of a power retained by the states:
*Pollock v. Farmers' Loan & Trust Co.,* 157 U. S. 429;
*Collector v. Day,* 11 Wall. 113;
*Indian Motorcycle Co. v. United States,* 283 U. S. 570.

*The Panhandle Oil Company case,* above cited, was an action to recover from the Oil Company a state excise tax on the sale of gasoline to the United States. The plea, which was demurred to, shows that the Oil Company had not included the tax in the sale price to the Government. The defense was sustained by this Court on the ground that the tax was a burden on or interference with the exertion of a national power. Not only had the United States not intervened in that case, but the dissenting opinion of Mr. Justice Holmes would seem to indicate that the right of the Oil Company to interpose the defense was at least considered by this Court.

In many cases, the United States would not be in a position to complain of state legislation at the time

necessary to protect its power. The burden on the performance of a governmental function, such as that in the case at bar, would operate as soon as the Government called for bids for materials to be sold to it or for work to be done for it.

The inhibition against state interference with the exercise of a federal function is based on the Constitution. Its violation is restrained as a matter of general right, where the complainant can show special interest in the preservation of the power, as where the impairment of the power would impede his right to deal with the federal government. This is peculiarly the case where the tax involved is a privilege tax and where the right to do business with the United States is conditioned on the payment of the tax, as in the case at bar.

The right of a citizen to deal with the United States does not depend on authority conferred by any State. When a State seeks to exact tribute as a condition to doing business with the federal government, its action will be restrained at the suit of the citizen who deals with the government without paying the tribute.

In the case of *Panhandle Oil Company v. Mississippi,* 277 U. S. 218, 221, Mr. Justice Butler in delivering the opinion of this Court said:

> "The petitioner's right to make sales to the United States was not given by the State and does not depend on state laws; it results from the authority of the national government under the Constitution to choose its own means and sources of supply."

The same fundamental principle was expressed by Chief Justice Marshall in delivering the opinion of this Court in the case of *McCulloch v. Maryland,* 4 Wheat. 316, 430, when he said:

> "The attempt to use it [state power of taxation] on the means employed by the government of the Union, in pursuance of the constitution, is itself an abuse, because it is the usurpation of a power which the people of a single state cannot give."

We submit, that the mere attempt of a State to impose conditions on the privilege of doing business with the United States can be restrained by the person who exercises or seeks to exercise the privilege.

The cases cited by appellant at pages 56 and 57 of his brief do not appear to us to decide definitely the proposition for which appellant contends. In the case of *General Construction Co. v. Fisher,* 149 Or. 84, 39 P. (2d) 358, the Supreme Court of Oregon held that a net income tax on a contractor doing work for the government was not "an unwarranted interference with a function of the federal government". The case may be disposed of by pointing out that a net income tax is indirect and remote and is not palpable and direct, like a gross income tax. It is true that in the course of a lengthy opinion the Court mentioned the fact that the federal government was not complaining and had not commissioned the plaintiff to intervene in its behalf.

The language quoted from the opinion in the case of *Meyer Construction Company v. Corbett,* 7 Fed. Supp. 616, should be confined to the facts with which the Court was dealing. Plaintiff was engaged in the performance of a construction contract for the United States. Plaintiff purchased supplies from a retailer who was required to pay a gross sales tax, which he apparently added to the selling price. Plaintiff sought to enjoin the collection of this tax. In as much as plaintiff had not paid the tax and in as much as it was not imposed upon his

receipts from materials furnished or services rendered to the United States, plaintiff had no standing to contest the tax. It is the same kind of tax as was involved in the case of *Trinityfarm Construction Company v. Grosjean,* 291 U. S. 466, which case was relied upon by the Court in its opinion. Our position in this respect is made clear from the following sentence in the opinion of the District Court in the *Meyer Construction Company case* quoted at page 57 of appellant's brief: "If this tax on retailers for the privilege of doing retail business is unconstitutional, the proper parties to raise the constitutional question are the parties upon whom the tax is levied."

The party upon whom the tax was levied was a retailer and not the Meyer Construction Company.

We can not see that the cases of *Silas Mason Company v. Henneford,* 15 Fed. Supp. 958, and *Trinityfarm Construction Company v. Grosjean,* 291 U. S. 466, even state, much less sustain, the principle for which appellant contends.

We submit that the appellee is a proper party to resist the exaction from it of a tax on the privilege of doing business with the United States.

The District Court correctly apprehended the fundamental fallacy of appellant's contention when it said that "the state of West Virginia has no power to impose upon and collect from the plaintiff this tax."

## II.

**The Tax Is Assessed, in Part, on Gross Income of a Foreign Corporation From Transactions Entirely Outside West Virginia and, Therefore, Violates the Due Process Clause of the Constitution.**

## III.

**The Tax Is Assessed, in Part, on Gross Income of a Foreign Corporation From Transactions in Interstate Commerce and, Therefore, Violates the Interstate Commerce Clause of the Constitution.**

These two propositions are so interrelated that we believe they can be argued together in the interest of brevity without sacrificing clarity.

It is established that, under the due process clause, a state may not levy a tax on the income of a foreign corporation from transactions entirely outside the state. *Hans Rees' Sons, Inc. v. North Carolina,* 283 U. S. 123; *Shaffer v. Carter,* 252 U. S. 37. A gross income tax on such income is invalid: *Meyer v. Wells, Fargo & Co.,* 223 U. S. 298.

It is also definitely established that a state may not levy a gross income tax on the income derived from transactions in interstate commerce.

*Fargo v. Michigan* (*Fargo v. Stevens*), 121 U. S. 230.

*Phila. & Southern Steamship Co. v. Pennsylvania,* 122 U. S. 326.

*Galveston, H. & S. A. Ry. Co. v. Texas,* 210 U. S. 217.

*Crew Levick Co. v. Pennsylvania,* 245 U. S. 292.

*Cudahy Packing Co. v. Minnesota*, 246 U. S. 450.
*New Jersey Bell Telephone Co. v. State Board of Taxes and Assessments*, 280 U. S. 338.

In *East Ohio Gas Co. v. Tax Commission*, 283 U. S. 465, 470, this Court said:

"It is elementary that a State can neither lay a tax on the act of engaging in interstate commerce nor on gross receipts therefrom."

Before proceeding further with this argument, however, we will undertake to answer, briefly, the first proposition of appellant's argument.

REPLY TO APPELLANT'S ARGUMENT, POINT I.

Appellant admits the legal propositions that the gross income of a foreign corporation, derived from extrastate transactions and from transactions in interstate commerce, is exempt from state taxation (Appellant's Brief, page 55). Appellant does not deny the fact that extrastate transactions and transactions in interstate commerce actually took place in connection with these contracts (Appellant's Brief, page 26).

Appellant attempts to escape, however, from the application of the rulings of the cases cited above, by the contention that the contracts here involved were purely local undertakings, and that the acquisition and fabrication of materials outside West Virginia and the interstate transportation that was involved were purely incidental to local undertakings (Point 2 of appellant's Statement of Points to be Relied Upon, appellant's brief, page 15; Summary of Argument I, *id.* page 16; Argument I, *id.*, page 20).

In other words, appellant contends that the things appellee was required to do and to furnish under these contracts were transactions entirely intrastate.

To sustain this contention, appellant first cites the case of *Western Gas Construction Co. v. Commonwealth,* 147 Va. 235, 136 S. E. 646, (affirmed in memorandum opinion, 276 U. S. 597-598, as holding "that the contract was not a transaction in interstate commerce but of a local construction" (appellant's brief, page 22). We submit that the case cited will bear no such construction. The question involved in that case was the liability of the construction company for a fine imposed for failure to secure a license to do the work required in the performance of a construction contract. The defense interposed was that the work required was purely interstate or entirely incidental to interstate commerce. The decision was that *some of the work* was purely local. A ruling as to whether *all of the work* was intrastate was neither required nor made.

Appellant then cites *General Railway Signal Co. v. Virginia,* 246 U. S. 500, *Kansas City Structural Steel Co. v. Arkansas,* 269 U. S. 148, *Browning v Waycross,* 233 U. S. 16, and *Interstate Construction Co. v. Lakeview Canal Co.,* 31 Wyo. 191, 224 Pac. 850, apparently as supporting the rule contended for. In each of those cases the issue was the liability of the defendant for fine or penalty for failure to secure a license to do the work required in a construction contract. Both intrastate and interstate commerce were involved under each contract. The defense in each case was that the statutory requirements constituted a burden on interstate commerce. In each case the court sustained the finding that intrastate or local work had been performed, separate and apart from interstate commerce. This was all that was required to sustain the fine or penalty.

None of the decisions in the cases under discussion, nor the opinions handed down therein, nor the excerpts from the opinions quoted by appellant, can be construed as holding that provisions for local work in a construction contract destroy the extrastate and interstate character of other transactions provided for therein. The only question involved in any of the cases cited by appellant and above discussed, was whether any work, however little, was local so as to sustain the license tax. We admit we did such local business and paid the tax. We contend, however, that a large part of our work was interstate or extrastate and that it could not be directly burdened by a gross income tax.

In fact, the very cases relied upon by appellant, when carefully analyzed, illustrate a proposition relied upon by appellee in this part of its argument. They decide that the inherent or essential nature of intrastate or local business is not lost because a construction contract also makes provision for interstate commerce. The obverse of this rule is that that which is inherently or essentially interstate is not lost because the construction contract also provides for intrastate or local business. In *York Manufacturing Co. v. Colley*, 247 U. S. 21, 26, Mr. Chief Justice White actually so construed the case of *Browning v. Waycross, supra*:

> "In fact, the case last referred to when looked at from a broad point of view is but an illustration of the principle applied in the *Waycross Case* to the effect that that which was inherently intrastate did not lose its essential nature because it formed part of an interstate commerce contract to which it had no necessary relation. And this truth by a negative pregnant states the obverse view that *that which is intrinsically interstate and immediately and inherently connected with interstate*

> *commerce is entitled to the protection of the Constitution* of the United States resulting from that relation." (Italics ours)

That a unitary business of a corporate enterprise may not be subjected to a net income tax by a state, in disregard of the extent to which its income is derived from the conduct of the enterprise in another state, was held in the case of *Hans Rees' Sons, Inc., v. North Carolina,* 283 U. S. 123. In delivering the opinion of this Court, Mr. Chief Justice Hughes said (page 133):

> "But the fact that the corporate enterprise is a unitary one, in the sense that the ultimate gain is derived from the entire business, does not mean that for the purpose of taxation the activities which are conducted in different jurisdictions are to be regarded as 'component parts of a single unit' so that the entire net income may be taxed in one State regardless of the extent to which it may be derived from the conduct of the enterprise in another State."

The application of these rules to the instant case is greatly strengthened by the nature and legal incidence of a gross income tax. Such a tax is a direct and immediate burden upon the business affected: *United States Glue Co. v. Oak Creek,* 247 U. S. 321, 328; it burdens every transaction in such business by withholding for the use of the state a part of every dollar received from such transactions: *Crew Levick Co. v. Pennsylvania,* 245 U. S. 292, 297; it is an exaction made out of commerce itself, it is a burden upon it, and seriously affects it: *Philadelphia & Southern Steamship Co. v. Pennsylvania,* 122 U. S. 326, 342, and other cases cited at pages 19-20 of this brief.

We therefore submit not only that the authorities cited by appellant fail to sustain the general proposition embodied in appellant's argument, Point I (appellant's brief, page 20), but also that these very authorities sustain the opposite position relied upon by appellee.

Counsel for appellant proceed (appellant's brief, page 26) to apply the "principles", deduced by them from the cases above discussed, to the case at bar and to conclude from that application that the tax in the instant case is claimed solely on account of the engaging by appellee in the business of contracting in West Virginia, and not at all on account of the extrastate activities and the activities in interstate commerce required of appellee in the performance of its contracts. The misconception as to the "principles" to be deduced from the cases relied upon invalidates the conclusion arrived at.

Appellant thereupon argues that, as there is nothing in the contracts themselves or in the invitations to bid specifying that any of the articles shall be obtained at any particular place either within or without the State of West Virginia, the interstate commerce transactions may be deemed merely incidental and may be disregarded in the decision of the case; citing *Wiloil Corporation v. Pennsylvania,* 294 U. S. 169.

This Court decided that the tax in the Wiloil case was a property tax. The decision was so construed in the case of *Henneford v. Silas Mason Co., Inc.* (Supreme Court of the United States No. 418 October Term 1936. Decided March 29, 1937). In delivering the opinion of the Court in that case, Mr. Justice Cardozo said:

> "Things acquired or transported in interstate commerce may be subjected to a property tax, non-

> discriminatory in its operation, when they have become part of the common mass of property within the state of destination. *Wiloil Corp. v. Pennsylvania,* 294 U. S. 169, 175; * * *"

This distinguishes the Wiloil case from the case at bar.

In addition, the Record shows that the contracts involved in the case at bar not only contemplated, but also necessarily involved or actually required interstate commerce.

For example, the United States knew prior to entering into the contracts that the roller gates, lock gates, parts, and other equipment and works incident thereto would be fabricated and manufactured at the plant and shops of appellee at Neville Island, Pittsburgh, Pennsylvania (R. 349-350). The bid on the London contract so specifies (R. 397). They were fabricated and manufactured there (R. 350). The London contract provides for complete assembly and the careful drilling, bolting, and match-marking of the gates in the shop (R. 220). There were similar provisions for the imbedded substructure rack and spur rim (R. 220). The appellee neither owns nor maintains any other shop (R. 346).

Running all through the London contract are references to the work to be done in the shop, viz., shop inspection (R. 148), painting (R. 155, 157, 177, 223, 226, 233, 240, 253 and 257). The London contract is typical of all the contracts (R. 427).

If these materials were to be purchased, fabricated, assembled, match-marked, inspected, and painted at Neville Island, Pennsylvania, and were later to be installed in locks and dams in West Virginia, the necessity of interstate commerce is manifest.

We submit that the following principles have been definitely established:

1. In general, a state may not impose a tax on transactions of a foreign corporation entirely outside the taxing state or in interstate commerce.

2. Even in an ordinary construction contract, the performance of local work within the taxing state does not give such state authority or power to tax a foreign corporation upon extra-state or interstate transactions arising out of the same contract.

3. A state tax even on net income of a unitary business of a foreign corporation in disregard of the extent to which said income is derived from the conduct of the business in another state is invalid.

4. The nature and the direct incidence of a gross income tax strengthens the applicability of the above rules to the case at bar.

**Contracts Did Involve Extrastate Transactions and Transactions in Interstate Commerce**

We now resume our argument at the point at which we digressed to reply to the first part of appellant's argument.

As previously stated, appellant does not appear to deny the facts in respect of extrastate transactions and transactions in interstate commerce under the contracts of appellee, but treats them as incidental. Despite this, we feel that this Court is entitled to a brief summary of the facts in the record indicating the nature and extent of these transactions.

EXTRASTATE TRANSACTIONS ON WHICH TAX IS IMPOSED

Appellee's undertaking under the four contracts involved was to "furnish all labor and materials, and perform all the work required for furnishing of labor and materials and performing all work" for the erection and construction of the respective locks and dams (R. 61).

The general specifications in the London contract describe the work to be done and the equipment to be furnished as (1) a 56 by 360 foot lock, complete with 2 miter gates, 4 gate operating machines, 2 Stoney gate valves, and necessary piping; (2) power house; (3) power house machinery for raising the roller gates; (4) electrical distribution system; and (5) a roller gate dam, consisting of five 100-foot by 26-foot steel gates closing on concrete sills between concrete piers and individually operated by electric hoists housed on the tops of the piers; and (6) steel service bridge of the deck-truss type approximately 565 feet in length and provided with a 30-ton revolving crane and a 30-ton bridge-crane unit (R. 98). The other contracts provided for comparable structures.

It is stipulated:

> "Plaintiff purchased outside of the State of West Virginia all materials used in the fabrication and manufacture of the roller gates, lock gates, cranes, substructure racks and spur rims, structural steel, patterns, hoisting mechanism and equipment under each of said contracts; and at its plant at Neville Island, Pittsburgh, Pennsylvania, fabricated and manufactured the same." (R. 350)

The United States knew at the time the contracts were entered into, by information furnished with the

bids for the respective contracts, that the roller gates, and the machinery and equipment connected therewith, would be fabricated and manufactured at appellee's Neville Island Shops (R. 349-350).

Partial payments were made from time to time for certain materials purchased by and delivered to plaintiff at its Neville Island Shops; also for certain articles and equipment manufactured or fabricated by plaintiff during the progress of the work (R. 357).

In the London contract, partial payments aggregating 50% of the unit price were provided for upon the fabrication of the roller gates, imbedded substructures, hoists, and lifting chains (R. 222).

The partial payments provided for were made (R. 357).

The London contract was typical of the other contracts (R. 427). All contained similar provisions. In the Winfield and Gallipolis contracts additional partial payments were provided for and made upon the delivery of materials at appellee's Neville Island shops (R. 358).

The contracts all contain the following provision (London contract, Article 16(c) (R. 68)):

> "All material and work covered by partial payments made shall thereupon become the sole property of the Government * * *."

This provision was effective to pass title to the United States for all material and work covered by the partial payments: *United States v. Ansonia Brass & C. Co.*, 218 U. S. 452. The ruling of the court in this connection is found at page 467 as follows:

> "But it is equally well settled that if the contract is such as to clearly express the intention of the

parties that the builder shall sell and the purchaser shall buy the ship before its completion, and at the different stages of its progress, and this purpose is expressed in the words of the contract, it is binding and effectual at law to pass the title. 2 Parsons on Contracts, 8th ed. 259, and cases cited."

The aggregate of the partial payments made by the United States under all four contracts to the appellee for work at appellee's Neville Island plant was $768,366.22 (R. 357-358).

*We respectfully submit that said sum received by appellee in Pennsylvania upon delivery of materials and upon fabrication of materials at its plants at Neville Island, Pennsylvania, was clearly income from transactions entirely outside the State of West Virginia.*

The above total, however, represents only partial payments and not the entire income properly attributable to the fabrication of the articles mentioned. It was impossible to determine and stipulate the total price paid for fabrication because of the use of unit prices, which included installation and erection.

There are, however, stipulated facts which serve to give some true index of the work done and materials purchased and fabricated at appellee's plant at Neville Island, Pennsylvania, (R. 370):

"(1) Cost of Materials, and Fabrication at Neville Island, Pennsylvania, Including Labor.

| | |
|---|---|
| "Marmet | $ 354,189.67 |
| "London | 425,723.76 |
| "Winfield | 270,546.15 |
| "Gallipolis | 390,582.10" |
| Total | $1,441,041.68 |

Appellee incurred other costs entirely outside West Virginia, such as insurance, drafting room expenses, executive overhead, etc. The aggregate cost to the appellee of these last mentioned items entirely outside West Virginia was $344,683.10 (R. 370).

Appellee secured the roller gate designs through an arrangement with the Krupp organization of Germany (R. 349). Royalties paid by appellee to Krupp amounted in the aggregate to $42,360.42 (R. 370).

Patterns made by appellee at Pittsburgh, Pennsylvania, for the roller gates and lock gates, as provided by three of the contracts, were delivered by appellee to the United States at the United States Repair Station at Marietta, Ohio (R. 357).

We submit that, under the due process clause of the Constitution of the United States, the gross income of appellee derived from transactions outside West Virginia was exempt from the gross income tax of West Virginia.

INTERSTATE COMMERCE ON WHICH TAX IS IMPOSED.

In each instance, the written contracts were mailed from Huntington, West Virginia, to the appellee at Pittsburgh, Pennsylvania, for execution, and were returned by mail to the United States Engineer Office at Huntington, West Virginia, for execution by the United States (R. 342).

In the preceding section we have indicated the extent of the purchases of materials for fabrication and the fabrication thereof at appellee's shops at Neville Island, Pennsylvania, the partial payments made, and the passing of title to said materials and fabricated materials, to the United States.

The machinery, equipment, and other materials purchased and fabricated in Pennsylvania, and dis-assembled into units when necessary, were shipped and transported by appellee, down the Ohio and up the Kanawha River, from Pennsylvania into West Virginia, by barge, to the respective dam sites (R. 351).

Other materials, including cement, re-enforcing steel, riprap, forms for coffer dams, timber, steel piling, bolts and washers, paint, corrugated sheets, and miscellaneous materials and supplies were purchased by appellee outside West Virginia and transported by rail or river from the place of purchase to the site of the particular work (R. 356). These materials were unloaded at the respective work sites and either installed in the locks and dams or stored on property of the United States (R. 356).

In addition to towboats and barges used in the transportation of materials and equipment as above set forth, derrick boats, mixer boats, scows and other river craft, fitted out with machinery and equipment, were taken from Pennsylvania for use at the work sites and were returned after the work was completed (R. 356, 360). This was interstate commerce strictly, the same as railroad or steamship carriage.

Partial payments were made on the delivery of materials at the respective work sites (R. 357-359). Under the provisions of the contracts (R. 68), title to the articles or materials covered by such partial payments, thereupon passed to the United States (see p. 47, *supra*).

*The foregoing transactions clearly constituted interstate commerce.*

In *Addyston Pipe & Steel Co. v. U. S.*, 175 U. S. 211, 241, this Court referred to prior decisions as establishing that

> "interstate commerce consists of intercourse and traffic between the citizens or inhabitants of different States, and includes not only the transportation of persons and property and the navigation of public waters for that purpose, but also the purchase, sale and exchange of commodities."

In *International Textbook Co. v. Pigg*, 217 U. S. 91, 107, this Court said:

> "'* * * Importation into one State from another is the indispensable element, the test, of interstate commerce; and every negotiation, contract, trade, and dealing between citizens of different States, which contemplates and causes such importation, whether it be of goods, persons, *or information*, is a transaction of interstate commerce.'"

In *Dahnke-Walker Milling Co. v. Bondurant*, 257 U. S. 282, 290, this Court said:

> "The commerce clause of the Constitution, Art. I, § 8, Cl. 3, expressly commits to Congress and impliedly withholds from the several States the power to regulate commerce among the latter. Such commerce is not confined to transportation from one State to another, but comprehends all commercial intercourse between different States and all the component parts of that intercourse."

In order to show the extrastate and interstate aspects of certain transactions required by these con-

tracts, let us follow the course of a typical fabricated article, a roller gate:

1. Steel purchased outside West Virginia (R. 350);
2. Fabricated at Neville Island, Pennsylvania (R. 350):
3. Assembled, inspected, and tested there (R. 350);
4. Partial payment (R. 344);
5. Title passed to the United States (R. 63);
6. Disassembled for shipment (R. 351);
7. Stored at Neville Island (R. 351);
8. Shipped by barge to dam site (R. 351);
9. Unloaded onto and into locks and dams (R. 351);

Down to this point the transactions are entirely extrastate or interstate.

10. Placed on foundations (R. 351).

### EXTRASTATE AND INTERSTATE TRANSACTIONS SUBSTANTIAL IN AMOUNT

As the London contract, only, is printed in the record, we will confine our statements to it, although the other contracts contain similar provisions.

We have mentioned above that this contract provided for the furnishing of five steel roller gates, each of which was 100 x 26 feet. The aggregate weight was approximately 225 tons per roller gate (R. 353). The unit price of each gate was $66,000, or a total of $330,000 (R. 394).

The service bridge was approximately 565 feet long (R. 98). The service bridge was made of structural steel, truss design (R. 353).

In addition to the foregoing, there were two miter gates (no unit price); two Stoney gate valves, aggregate unit price $24,000; four lock gate operating machines, aggregate unit price $14,000; power house machinery, unit price $19,000; electrical revolving locomotive crane, unit price $25,000; electric bridge-crane unit, unit price $7,500; electric wiring illumination and control equipment, unit price $19,800; and other articles (R. 394).

All of the above described machinery and equipment was purchased or manufactured outside and transported into West Virginia.

We have stated previously (page 48) that the partial payments made by the United States to the appellee under the four contracts for materials delivered at Neville Island and for materials purchased and fabricated at Neville Island aggregated $768,366.22. Additional partial payments were made upon delivery of the fabricated materials at the respective sites of the work at Marmet and London in the aggregate amount of $93,288 (R. 357). Additional partial payments were made upon the delivery of other materials at the respective work sites aggregating, under the four contracts, $304,143.96 (R. 358-359). The total of all partial payments made upon delivery of materials at the respective work sites was $397,431.96.

The total of the partial payments directly attributable to transactions in interstate commerce was $1,165,798.18.

As above stated, the foregoing substantial amounts represent partial payments only. They do not represent the entire income properly attributable to interstate commerce. The following figures represent the cost

totals of the corresponding figures for each contract (R. 370):

| | | |
|---|---|---|
| 1. | Cost of materials and fabrication at Neville Island, Pennsylvania, including labor | $ 1,441,041.68 |
| 2. | Cost of other materials purchased outside West Virginia | 1,707,102.65 |
| 3. | Transportation cost of haulage in interstate commerce | 118,022.74 |
| | Total | $ 3,266,167.07 |

We have included in the above costs of transactions in interstate commerce, the cost of materials and fabrication at Neville Island, Pennsylvania.

Not included, however, in the foregoing figures is the item of $685,573.21 for the rental of plant and equipment transported by river from Pennsylvania into West Virginia and returned after the completion of the jobs.

The foregoing facts and figures conclusively answer appellant's statement (appellant's brief, page 43):

> "Certainly, if its activities are otherwise taxable, as we contend they are, the appellee cannot seek immunity from the West Virginia gross sales and income tax merely by introducing one or a few articles in the performance of a large contract, the handling of which articles might possibly be viewed as an act of interstate commerce."

We submit that, under the commerce clause of the Constitution of the United States, the gross income of appellee derived from transactions in interstate commerce was exempt from the gross income tax of West Virginia.

THE TAX IS IMPOSED ON RECEIPTS FROM EXTRASTATE AND INTERSTATE TRANSACTIONS

Having shown the nature and extent of the extrastate and interstate transactions, we should logically be required to demonstrate that the taxed income includes the receipts from such transactions. This is fully covered by the stipulation (R. 374):

"The gross income received by the plaintiff from the United States during the years 1933 and 1934 under the said government contracts and during the progress of the work thereunder, was the amount agreed to be paid to the plaintiff by the United States by the terms of said contracts, and was the amount of the bids by the plaintiff for performing said contracts, or for any additional work required by the United States in compliance with said contracts. Competent witnesses for the plaintiff, if called, would testify:

"Said bids by the plaintiff ('Appendix B') for each of the respective four contracts were based upon the actual estimated cost of the following items: materials, labor, tools and supplies; transportation of equipment, materials and supplies; superintendence, time keeper and engineering; watchmen, tool house men, water boys, etc.; compensation and liability insurance, construction bond and property taxes; other small incidental expenses. There was also taken into consideration an amount for plant rental on the equipment to be used, based on the valuation of the plant depreciation, repairs and insurance, and cost of rented equipment. In addition to the above items, there was included in the calculations and estimates for the bids the cost of the work at the shops at Neville Island, including actual estimated cost of labor,

including shops and drawing rooms; actual estimated cost of materials; and overhead costs, based on percentage of direct labor."

The definition of "gross income" in the Gross Sales and Income Tax Law of West Virginia involved in this case seems pertinent at this point (R. 27):

"'Gross income' means the gross receipts of the taxpayer received as compensation for personal services and the gross receipts of the taxpayer derived from trade, business, commerce or sales and the value proceeding or accruing from the sale of tangible property (real or personal), or service, or both, * * * and without any deductions on account of the cost of property sold, the cost of materials used, labor costs, taxes, royalties, interest or discount paid or any other expense whatsoever."

The tax assessed in this case was based upon the entire gross income of appellee, as above defined, for the years 1933 and 1934. The income thus assessed included the income derived from extrastate transactions and from transactions in interstate commerce. The assessment as made cannot be sustained. *Cooney v. Mountain States Telephone & Telegraph Co.*, 294 U. S. 384. In delivering the opinion of the Court in that case, Mr. Chief Justice Hughes said (p. 392-393):

"But a State cannot tax interstate commerce; it cannot lay a tax upon the business which constitutes such commerce or the privilege of engaging in it. *And the fact that a portion of a business is intrastate and therefore taxable does not justify a tax either upon the interstate business or upon the whole business without discrimination.* * * * Where the tax is exacted from one doing both an

interstate and intrastate business, it must appear that it is imposed solely on account of the latter; that the amount exacted is not increased because of the interstate business done; * * *." (Italics ours.)

**REPLACEMENTS AND IMPROVEMENTS IN THE CANALIZATION OF A NAVIGABLE RIVER CONSTITUTE, IN THEMSELVES, WORK IN INTERSTATE COMMERCE**

As we have heretofore pointed out (page 21 hereof), the Kanawha River had been improved for navigation for many years before the construction of the locks and dams covered by the contracts involved in this case. There were already ten locks and dams on the river, affording a six foot channel. The four new locks and dams were designed to, and did, take the place of those ten locks and dams and afforded a nine foot channel. The first contract, entered into on August 30, 1932, was for the construction of the lock and dam at Marmet. The General Specifications are headed "Maintenance and Improvement of Existing River and Harbor Works" (R. 428). The appellee was required by the contracts so to proceed with its work as not to interfere with the passage of river craft on the existing channel and through the old locks during the construction of the new locks and dams. The London contract provided that "the upper pool will be maintained not lower than elevation 603.0 in order to permit navigation over the upper sill of Lock 'B'." (R. 104). At Marmet, the old dam was about nine hundred feet below the new dam. It was necessary there to connect up the channel side of the new lock with the old dam so as to hold the water in the upper pool. The part of the old dam so replaced was then blasted out, so as to permit vessels to move from the new lock to the channel. Later, when the new dam was constructed, the

second coffer dam had to be constructed so as to form the dam for the upper pool, so that river craft could move through the existing lock while the dam was being constructed. Provision for this was made in the Marmet contract, General Specifications, paragraph 12, entitled "Order of Work". The Marmet contract was attached to the Stipulation as Exhibit 3, but was omitted in the printing of the Record (Record Index, Exhibit 3).

The situation is, therefore, different than that presented in the canalization of a river not already navigable in fact by large boats.

The work done was the improvement of an artery of commerce, while a stream of traffic was flowing through the artery. The work may be compared to the repair of a railroad bridge on an interstate railroad. A workman engaged on such work has been held to be engaged in interstate commerce. *Pederson v. D. L. & W. R. Co.*, 229 U. S. 146. The case of *Raymond v. Chicago, M. & St. P. Ry. Co.*, 243 U. S. 43, might be cited to the effect that the construction of a tunnel to be used by an interstate railroad company, when completed, was not interstate commerce. We do not contest that proposition. On the contrary, it emphasizes the distinction we are endeavoring to draw, namely, that work in the improvement, replacement, or repair of an interstate railroad is interstate commerce, while the construction of a new railroad, or tunnel or bridge therefor, is not, or may not be, interstate commerce. So, work done in the canalization of a river not theretofore navigable in fact would not be work done in interstate commerce, as would work done in deepening of an existing channel and the replacement of existing locks and dams, while boats moved up and down the river.

The very construction of these dams, regardless of state boundaries, was, therefore, work in interstate commerce which can not be impeded or burdened with a gross income tax on the moneys paid by the Government for the materials delivered and work done.

**The Tax Cannot Be Apportioned to Receipts From Local Business Under the Statute and the Facts**

Appellant, apparently recognizing the unsoundness of his position that the entire assessment against the appellee is valid, shifts his position and suggests the application of the act to appellee's intrastate or local business in the event that the assessment in its entirety cannot be sustained (see argument, Part IV, Appellant's brief, page 41 *et seq.*).

Appellant argues that "said tax is susceptible of division relative to the part of the receipts from business done within the State and the part from business done without the State" (appellant's brief, page 42). In support of this position, appellant cites *Singer Sewing Machine Co. v. Brickell,* 233 U. S. 304. The tax involved in that case was a flat rate tax for each county in which sewing machines were sold. The Singer Sewing Machine Company, claiming that part of its business was interstate and part intrastate, sought total exemption from the tax. The act was construed as applicable only to counties where intrastate business was done.

Appellant also relies on *Crew Levick Co. v. Pennsylvania,* 245 U. S. 292. The record in that case clearly disclosed the intrastate income subject to the tax and that part of the tax was uncontested.

The statute in suit makes no provision for apportionment of the tax as between extrastate and inter-

state commerce on the one hand and intrastate commerce on the other. That omission is expressly admitted in defendant's answer (R. 329, 333).

The statute gives no authority to the Tax Commissioner to make such apportionment or even to make rules and regulations under which such an apportionment can be effected.

Under these circumstances the tax is unenforceable against the intrastate or local business which it might have reached, had it been drawn otherwise, for to permit the Tax Commissioner to devise some system of apportionment would constitute legislation by an administrative officer. *Porto Rico Mercantile Co. v. Gallardo,* 6 F. (2d) 526; *Commonwealth v. P. Lorillard Co.,* 129 Va. 74, 105 S. E. 683. In *Meyer v. Wells, Fargo & Co.,* 223 U. S. 298, 302, this Court said:

> "Neither the court below nor this court can reshape the statute simply because it embraces elements that it might have reached if it had been drawn with a different measure and intent."

The rule stated is subject to an exception where the record clearly discloses a basis for apportionment. *Western Union Telegraph Co. v. Ratterman,* 127 U. S. 411. Appellant does not claim that the record in the case at bar furnishes any such basis.

Another exception to the rule occurs when the subject matter of the tax permits division or apportionment. *Bowman v. Continental Oil Co.,* 256 U. S. 642.

The taxed income in the case at bar is not susceptible of such division. The taxed income consisted of the aggregate of the unit prices provided for in the contracts multiplied by the number of units furnished. Most, if not all, of the unit prices included installation in

West Virginia, as well as the purchase and fabrication of the materials in Pennsylvania or elsewhere and the transportation thereof to the work sites (London contract, general specifications, Paragraph 13, R. 106, and unit prices bid by appellee, R. 393-395).

As an example, the service bridge in the London contract was a steel bridge of the deck-truss type, approximately 565 feet in length (R. 98). The unit prices, however, covering the service bridge installed, were based on pounds of steel, bolts, and similar materials (R. 393-395).

The figures given in the stipulation furnish no basis for apportionment, as they relate to costs and not to income.

We submit

1. That a large amount, in number and value, of the transactions, the receipts from which are assessed with the tax in suit, were performed and, in many instances, paid for in part outside West Virginia;

2. That a large amount, in number and value, of such transactions constituted interstate commerce;

3. That the tax is assessed against all receipts from such transactions commingled with receipts from local operations;

4. That the essentially extrastate and interstate character of certain operations is not lost because of the provisions for local construction;

5. That the tax cannot be applied in respect of the local operations alone;

6. That the construction of the locks and dams was, of itself, work in interstate commerce; and

7. That the entire assessment is, therefore, invalid.

## IV.

### A Substantial Part of the Work Was Done on Property Over Which the United States Had Exclusive Legislative Jurisdiction

While this proposition was advanced and argued in the District Court, it was not discussed or passed on by that Court. It is dealt with under heading III at page 33 of Appellant's brief. We shall state our position as briefly as we can.

The proposition becomes immaterial if this Court sustains the conclusion of the District Court that the tax is an unconstitutional burden on Government contracts, or, if the Court holds that the tax in suit violates the due process clause or the interstate commerce clause of the Constitution, in so far as it is imposed on the gross receipts from the contracts in suit.

If the proposition above stated is correct, West Virginia can not tax payments for machinery delivered and work done on land purchased by the United States on the opposite banks of the Kanawha at the respective dam sites.

Operations on land which is not within the legislative jurisdiction of West Virginia can not be taxed by it any more than Virginia could tax operations in the District of Columbia.

It is stipulated that the United States is the owner in fee simple, by purchase or condemnation, of land within the exterior boundaries of the State of West Virginia at the places where the said locks and dams were constructed and on a part of which said locks and dams were erected (R. 381). The United States owned

in fee 8.05 acres on the right bank and 11.86 acres on the left bank of the Kanawha River at Marmet; 3.2 acres on the right bank and 7.5 acres on the left bank at London; 23.49 acres on the right bank and 14.62 acres on the left bank at Winfield; and 9.54 acres on the right bank (in Ohio) and 59.72 acres on the left bank at Gallipolis (R. 381). Except in the one instance noted, all of this land is within the geographical boundaries of the State of West Virginia. "The United States purchased or acquired said lands for the purpose of the erection of said locks and dams" (R. 381). A deed, which is typical of the other deeds of conveyance to the United States, appears in the Record at page 403. It will be observed that this deed is a voluntary conveyance for a named consideration and conveys a fee simple title to the United States. It appears to have been duly recorded (R. 405).

West Virginia gave its consent to the acquisition by the United States, by purchase, condemnation, or otherwise, of any land for sites for locks and dams or other purposes (West Virginia Code 1931, Chapter 1, Article 1, Section 3, Appendix hereto page 71).

Article I, Section 8, Clause 17, of the United States Constitution confers on Congress the power to exercise exclusive legislation "over all places purchased [by the United States] by the consent of the legislature of the state in which the same shall be, for the erection of forts, magazines, arsenals, dock-yards, and other needful buildings." That locks or dams are "needful buildings" within Clause 17 is held in *United States v. Tucker,* 122 Federal Reporter 518, 522, in a well considered opinion of the District Court of the United States for the Western District of Kentucky. They are *ejusdem generis* as a dockyard.

A postoffice has been held to be a "needful building", under Clause 17, because it is erected in the exercise of the governmental function to establish postoffices. In the case of *Battle v. United States,* 209 U. S. 36, Mr. Justice Holmes, in delivering the opinion of this Court, said (page 37):

> "There can be no doubt of the power of Congress to purchase land within a State for postoffices or courts, by consent of the legislature of the State, and to exercise exclusive legislation over the same. Postoffices are among the 'other needful buildings' for the erection of which, as well as of 'forts, magazines, arsenals, dock-yards,' it is assumed that land will be bought, and for which land has been bought by the Government all over the United States. * * * The power to establish postoffices is given by Art. 1, § 8, cl. 7, in terms."

The construction of locks and dams is within the constitutional functions of the Federal Government; *Ashwander v. Tennessee Valley Authority.* 297 U. S. 288, 330.

As to the contention of the appellant that the construction of the dams in such manner that the water power thereby developed could be used for the generation of electric energy for commercial use deprived the dams of the character of "other needful buildings", little argument is necessary on our part.

This contention of the appellant is refuted by the decision of this Court in the case of *New York ex rel. Rogers v. Graves, et al., Tax Commissioners,* No. 139 October Term, 1936, decided January 4, 1937, in which this Court said through Mr. Justice Sutherland:

> "The primary purpose of the enterprise being legitimately governmental, its incidental use for

private purposes affords no ground for objection. *United States v. Chandler-Dunbar Water Power Co.*, 229 U. S. 53, 73; *Ashwander v. Tennessee Valley Authority*, 297 U. S. 288, 333."

The conclusion is inescapable that the locks and dams under consideration come within the phrase "other needful buildings" as used in Clause 17.

It seems clear, therefore, that Congress acquired exclusive legislative jurisdiction over the land purchased by the United States on the opposite banks of the river at the sites of the four locks and dams.

We do not understand that counsel for appellant contest the correctness of the proposition we have stated.

Their contention as set forth in the heading at page 33 of their brief is, as follows:

> "The contracts of appellee with the United States were not wholly performed on lands acquired by purchase or condemnation for the United States for needful buildings, but in part upon lands belonging to the State of West Virginia and subject to the jurisdiction thereof. The appellee is not exempt from West Virginia taxation."

It would seem, therefore, that counsel for appellant admit that part of the materials were delivered and part of the work was done on land over which the United States had exclusive jurisdiction. This being an admitted as well as a demonstrated fact, the conclusion is inevitable that West Virginia has no power to impose a tax on the doing of work or the delivery of materials on land over which it had no legislative jurisdiction whatsoever.

The cases cited by appellant do not attack or attemp to refute this proposition.

The case of *Ralph Sollitt & Sons Construction Company v. Commonwealth,* 161 Va. 854, 172 S. E. 290, merely held that the contractor, who was building a post-office, was subject to a small license tax on foreign corporations doing business in the State, because part of the work was done on the sidewalks surrounding the government property. It did not involve a gross income tax on the entire contract and work done and materials furnished thereunder, such as is involved in the case at bar.

The case of *Ohio River Contract Company v. Gordon,* 244 U. S. 68, held that, where a Government contractor building a canal on Government property had used other property for dumping material, the contractor had engaged in business in the State of Kentucky and was subject to suit there on a transitory action for personal injuries to an employee. This case would be authority for the proposition that the appellee could have been sued in the state courts of West Virginia in a transitory action because it did some business, however little, on property not owned by the United States.

We admit without hesitation that the appellee used some leased land in West Virginia, for storage and other purposes, not owned by the United States. This fact may have rendered the appellee liable to pay the license fee required of foreign corporations. It paid that fee (R. 383). We also admit that West Virginia could have assessed an *ad valorem* property tax on the property of the appellee in that State. Such a tax was so assessed and paid (R. 385). We say, however, that the fact, that

the appellee did some work or stored some materials on property over which the Government did not have exclusive jurisdiction, does not justify the State of West Virginia in assessing a gross income tax against receipts for materials delivered and work done, in substantial amounts, on land over which the United States did have exclusive legislative jurisdiction.

Appellee, "in the performance of its work in the years 1933 and 1934, in the construction of said locks and dams, used and occupied only that land on the banks of said rivers owned by the United States [except leased lots at three of the dam sites used for a roadway, storage, or temporary buildings] and also the beds of said rivers." (R. 382). No part of the locks or dams is located on the leased lots mentioned in the exception (R. 382).

A large part of what may be classified as local business, such as excavation, erection of concrete foundations, walls, and emplacements, and storage of materials, was done on land on the river banks purchased by the United States (R. 351, 352, 356).

As we have heretofore shown (see pages 56, 59 hereof), where a gross income tax is assessed by a state indiscriminately on income which the state is authorized to tax and on income which it is not authorized to tax, the court will strike down the entire assessment.

In other words, even if it should be admitted (which it is not) that West Virginia had the right to impose a gross income tax on receipts from materials delivered and work done on land over which the United States did not have exclusive jurisdiction, no basis would thereby be established to sustain such a tax on mate-

rials delivered and work done on land over which the United States had exclusive jurisdiction. If the tax is assessed indiscriminately on receipts from both such sources, without allocation, it must fall in its entirety.

Appellant's entire contention on this point is that title to the bed of the Kanawha River was in West Virginia, that the bed thereof, where parts of the locks and dams were constructed, had not been purchased by the United States, and that it did not have exclusive legislative jurisdiction thereover (Appellant's Brief pages 39 and 40).

Even if this be true, it in no way refutes our contention that the banks of the river, at the respective sites, were under the exclusive jurisdiction of the United States.

There can be no doubt that the Federal Government owns a dominant easement over navigable streams. *Gibson v. United States,* 166 U. S. 269, 271-272. Where it utilized that easement for the construction of locks and dams, there can be no doubt that it owned the land on which they were in part located; otherwise, West Virginia would have owned those parts of the locks and dams which were in the bed of the river.

Furthermore, when the United States exercised a constitutional power to construct the locks and dams, there can be no doubt that the means or method adopted for their construction can not be burdened or impeded by state legislation, imposing a tax or otherwise, as demonstrated herein under the heading at page 24. The inability of a state to enact legislation interfering with the exercise of a governmental function on land owned by the United States, however acquired, is affirmed in the case of *Fort Leavenworth R. R. Co. v.*

*Lowe,* 114 U. S. 525, 539. This phase of the question, however, goes beyond the proposition which we started out to support under this heading.

We, therefore, submit that the assessment of the Gross Sales and Income Tax of West Virginia against receipts from work done and materials delivered on the land purchased by the United States on the river banks at the sites of the locks and dams can not be sustained, even though a portion of the tax could be sustained if it had been assessed only against receipts from work done and materials delivered on other land.

## CONCLUSION.

We, therefore, respectfully submit:

FIRST: The tax, assessed by West Virginia against the gross receipts of the appellee from the United States under the four contracts, is a direct burden on, and impediment to, the privilege of doing business with the United States when exercising a governmental function; and the District Court properly restrained the collection thereof.

SECOND: The said tax assessment is a direct burden on extrastate and interstate business. It, therefore, violates the due process clause and the interstate commerce clause of the Constitution of the United States.

THIRD: As the tax is assessed indiscriminately against gross receipts from extra and interstate business and receipts from intrastate business, the Court will not attempt to allocate the tax to intrastate business and the entire tax must fall.

FOURTH: A substantial part of the tax is assessed against gross receipts from materials delivered and work done on property purchased by the United States and over which it had exclusive legislative jurisdiction. Regardless of other considerations, the assessment, being unlawful in part and not being itemized, is invalid altogether.

Respectfully submitted,

WILLIAM S. MOORHEAD,
LAWRENCE D. BLAIR,
W. CHAPMAN REVERCOMB,
W. ELLIOTT NEFFLEN,
*Counsel for the Appellee,*
*The Dravo Contracting Company.*

## APPENDIX.

### West Virginia Code 1931, Chap. 1, Art. 1, Secs. 3 and 4.

"Sec. 3. ACQUISITION OF LANDS BY UNITED STATES; JURISDICTION.—The consent of this State is hereby given to the acquisition by the United States, or under its authority, by purchase, lease, condemnation, or otherwise, of any land acquired, or to be acquired in this State by the United States, from any individual, body politic or corporate, for sites for lighthouses, beacons, signal stations, post offices, customhouses, courthouses, arsenals, soldiers' homes, cemeteries, locks, dams, armor plate manufacturing plants, projectile factories or factories of any kind or character, or any needful buildings or structures or proving grounds, or works for the improvement of the navigation of any watercourse, or work of public improvement whatever, or for the conservation of the forests, or for any other purpose for which the same may be needed or required by the government of the United States. The evidence of title to such land shall be recorded as in other cases.

"Any county, magisterial district or municipality, whether incorporated under general law or special act of the legislature, shall have power to pay for any such tract or parcel of land and present the same to the government of the United States free of cost, for any of the purposes aforesaid, and to issue bonds and levy taxes for the purpose of paying for the same; and, in the case of a municipal corporation, the land so purchased and presented may be within the corporate limits of such municipality or within five miles thereof: *Provided, however,* That no such county, magisterial district or municipality shall, by the issue and sale of such bonds, cause the aggregate of its debt to exceed the

limit fixed by the Constitution of this State: *Provided further,* That the provisions of the Constitution and statutes of this State, or of the special act creating any municipality, relating to submitting the question of the issuing of bonds and all questions connected with the same to a vote of the people, shall, in all respects, be observed and complied with.

"Concurrent jurisdiction with this State in and over any land so acquired by the United States shall be, and the same is hereby, ceded to the United States for all purposes; but the jurisdiction so ceded shall continue no longer than the United States shall be the owner of such lands, and if the purposes of any grant to the United States shall cease, or the United States shall for five consecutive years fail to use any such land for the purposes of the grant, the jurisdiction hereby ceded over the same shall cease and determine, and the right and title thereto shall reinvest in this State. The jurisdiction ceded shall not vest until the United States shall acquire title of record to such land. Jurisdiction heretofore ceded to the United States over any land within this State by any previous acts of the legislature shall continue according to the terms of the respective cession. (1881, c. 20, Sec. 4; 1909, c. 61; 1917, 2nd Ex. Sess., c. 5; Code 1923, c. 1, Sec. 4.)

"Sec. 4. EXECUTION OF PROCESS AND OTHER JURISDICTION AS TO LAND ACQUIRED BY UNITED STATES.—The State of West Virginia reserves the right to execute process, civil or criminal, within the limits of any lot or parcel of land heretofore or hereafter acquired by the United States as aforesaid, and such other jurisdiction and authority over the same as is not inconsistent with the jurisdiction ceded to the United States by virtue of such acquisition. (1881, c. 20, Sec. 5; Code 1923, c. 1, Sec. 5.)

# REPLY BRIEF

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IN THE

# Supreme Court of the United States

OCTOBER TERM, 1937

NO. 3.

ERNEST K. JAMES, Individually and as State Tax Commissioner of the State of West Virginia,
Appellant,

v.

THE DRAVO CONTRACTING COMPANY.

## REPLY BRIEF FOR APPELLEE ON REARGUMENT.

WILLIAM S. MOORHEAD,
LAWRENCE D. BLAIR,
W. CHAPMAN REVERCOMB,
W. ELLIOTT NEFFLEN,
*Counsel for the Appellee,*
*The Dravo Contracting Company.*

SMITH BROS. CO. INC., LAW PRINTERS, 208-212 GRANT STREET, PITTSBURGH, PA.

## SUBJECT INDEX.


PAGE

Summary of Argument ..... 1

Argument ..... 6

Questions Propounded ..... 6

Preliminary Statement ..... 6

I. A. Does the Gross Sales and Income Tax of West Virginia Impose a Direct Burden Upon the United States in the Exercise of a Constitutional Function? ..... 8

The Brief of the Attorney General Admits, in Effect, That It Does ..... 8

The Burden on the United States of Taxes of the Kind Involved in Suit Would Be Heavy ..... 11

The Attorney General's Proposition Is That It Is Immaterial Whether or Not the Tax in This Case Is a Burden on the Government ..... 11

The Enforcement of the Tax Statute in Suit Would Have Resulted in an Actual Interference With the Performance of a Governmental Function ..... 14

A Retroactive Gross Receipts Tax Would Seriously Impede the Performance of a Federal Function ..... 18

B. The Distinction Between Taxes Which Impose a Direct and Immediate Burden and Those Whose Effect Is Remote and Incidental Is Firmly Established and Is Reasonable and Practical ..... 19

PAGE

The Distinction Between Different Types of Taxes Is Reasonable and Practical..... 31

C. "The States Have No Power, by Taxation or Otherwise, to Retard, Impede, Burden, or in Any Manner Control, the Operations of the Constitutional Laws Enacted by Congress to Carry Into Execution the Powers Vested in the General Government"..... 37

Discrimination as Sole Test Violates Fundamental Principles ..... 37

The Exercise of a Constitutional Power by the United States Is Beyond the Jurisdiction of State Taxation ..... 40

Intergovernmental Tax Immunity Is Not Involved ..... 45

D. The Invalidation of Gross Receipts Taxes Assessed Against Government Contracts Works No Injustice to the States..... 46

The Concept of the Attorney General Is Conceptualistic and Unreal ..... 49

The Attorney General Does Not Propose That the States Shall Receive Much, if Any, Benefit From Gross Receipts Taxes on Federal Contracts ..... 51

II. The United States Had Exclusive Jurisdiction Over the Sections of the River Banks and the River Beds on Which the Locks and Dams Were Constructed..... 53

A. The Attorney General Agrees That the United States Had Exclusive Jurisdiction

PAGE

Over the Land Acquired by It on the River Banks ..... 53

The Wording of the West Virginia Consent Statute Shows That It Contains No Qualification to the Consent Therein Given ..... 55

B. The United States Had Exclusive Jurisdiction Over Those Parts of the River Beds on Which Portions of the Locks and Dams Were Constructed ..... 57

(1) There Was a Purchase by the United States Within the Meaning of the Constitution of the Sections of the River Beds on Which Portions of the Locks and Dams Were Constructed ..... 59

The Appropriation by the United States of Sections of the River Beds Under a Dominant Right Is Essentially the Same as the Acquisition of Land by Condemnation ..... 61

(2) The West Virginia Consent Statute Gives Consent to the Acquisition of the Sections of the River Beds on Which Portions of the Locks and Dams Were Constructed ..... 64

III. The Tax Is Assessed Without Apportionment Upon the Entire Gross Income of a Foreign Corporation From Business Conducted Partly in the Taxing State and

PAGE

Partly Outside the Taxing State and Partly in Interstate Commerce. Such an Assessment Violates the Due Process Clause and the Interstate Commerce Clause of the Constitution ..... 67

Income Taxation by a State of the Entire Income, Without Apportionment, of a Foreign Corporation From a Business Conducted Partly in the Taxing State and Partly in Another, Is Invalid..... 71

Interstate Commerce ..... 73

Impossibility of Apportionment of Tax to Income From Business in West Virginia... 73

Costs ..... 74

Conclusion ..... 75

## Table of Cases.

Alward v. Johnson, 282 U. S. 509..... 46

Bank of New York v. Hoffman, Mayor, et al., 7 Wall. 16 ..... 41

Brown v. Maryland, 12 Wheat. 419, 444..... 30

Brush v. Commissioner of Internal Revenue, 300 U. S. 352 .....22, 40

Burt v. Merchants' Insurance Co., 106 Mass. 356... 59

Choctaw, Oklahoma & Gulf Railroad Co. v. Harrison, 235 U. S. 292.....22, 26

Crandall v. Nevada, 6 Wall. 35, 44-46..... 39

Crew Levick Co. v. Commonwealth of Pennsylvania, 245 U. S. 292, 297.....21, 24, 73

PAGE

Educational Films Corp. v. Ward, 282 U. S. 379.... 21

Flint v. Stone-Tracy Co., 220 U. S. 107..... 21
Fox Film Corp. v. Doyal, 286 U. S. 123..... 21
Frick v. Pennsylvania, 268 U. S. 473, 494..... 29

Galveston, H. & S. A. Ry. Co. v. Texas, 210 U. S. 217 73
Gibson v. United States, 166 U. S. 269..... 60
Gillespie v. Oklahoma, 257 U. S. 501, 505.....26, 29, 39
Graves v. Texas Co., 298 U. S. 393.....30, 45

Hans Rees' Sons, Inc. v. North Carolina, 283 U. S. 123 ..... 72
Home Insurance Co. v. New York, 134 U. S. 594.... 21

Indian Motocycle Co. v. United States, 283 U. S. 570 .....30, 39, 45
Indian Territory Illuminating Oil Co. v. Oklahoma, 240 U. S. 522.....26, 39

Jaybird Mining Co. v. Weir, 271 U. S. 609, 613..... 29
Johnson v. Maryland, 254 U. S. 51.....10, 38, 39

Looney v. Crane Co., 245 U. S. 178..... 72

McCulloch v. Maryland, 4 Wheat. 316.....
.....10, 15, 29, 37, 38, 39, 42-44
Meyer v. Wells, Fargo & Co., 223 U. S. 298.....72, 73

New Jersey Bell Telephone Co. v. State Board, 280 U. S. 338, 346..... 21
Northwestern Mutual Life Insurance Co. v. Wisconsin, 275 U. S. 136.....20, 21, 26

Panhandle Oil Company v. Mississippi, 277 U. S. 218, 222 .....28, 30, 40, 45
The Pullman Co. v. Kansas, 216 U. S. 56..... 72

PAGE

Scranton v. Wheeler, 179 U. S. 141, 159 ..... 63
Shively v. Bowlby, 152 U. S. 1 ..... 65
Sinks v. Reese, 19 Ohio St. 306 ..... 54
Stewart Dry Goods Co. v. Lewis, 294 U. S. 555 ..... 23
Stockton v. Baltimore & N. Y. R. Co., et al., 32 Federal Reporter 9, 140 U. S. 699 ..... 63

Taber v. Indian Territory Illuminating Oil Co., 300 U. S. 1 ..... 23, 40
Telegraph Co. v. Texas, 105 U. S. 460 ..... 29
Trinityfarm Construction Co. v. Grosjean, 291 U. S. 466, 471, 472 ..... 27

Union Pacific Railroad Co. v. Peniston, 18 Wall. 5, 37 ..... 28
United States v. Baltimore & Ohio R. Co., 17 Wall. 322, 327 ..... 39
United States v. Cornell, 2 Mason 60, at 66 ..... 54
United States v. Tucker, 122 Fed. 518 ..... 59
United States Glue Co. v. Town of Oak Creek, 247 U. S. 321, 328-329 ..... 21, 23, 37

Wagner v. City of Covington, 251 U. S. 95, 102 .... 29
Western Union Telegraph Co. v. Kansas, 216 U. S. 1 72
Weston v. Charleston, 2 Peters 449 ..... 10, 39

**Table of Statutes and Constitutional Provisions.**

West Virginia Gross Sales and Income Tax Law, West Virginia Code of 1931, Chapter 11, Article 13, as amended May 26, 1933 . . 8, 11, 18, 19, 52, 54, 75
West Virginia Law dealing with acquisition of lands by the United States, West Virginia Code 1931, Chapter 1, Article 1, Sections 3 and 4 ..... 53, 54, 55, 56, 64, 66

*Table of Statutes and Constitutional Provisions.*


PAGE

Constitution of the United States:
- Fourteenth Amendment, Due Process Clause ..... 4, 57, 67, 72, 73, 75
- Article 1, Section 8, Clause 3, Interstate Commerce Clause ..... 4, 48, 67, 73, 75
- Article 1, Section 8, Clause 17, dealing with the exclusive legislative power of Congress ..... 3, 4, 53, 55, 58, 59, 60, 61, 66

North Carolina Emergency Revenue Act of 1937, Article V, Schedule E, Section 401 ..... 32

Opinions of the Attorney General:
- 7 Op. A. G. 114 ..... 59
- 10 Op. A. G. 34 ..... 54

Text Books:
- Cooley on Taxation (3d ed.), p. 1095 ..... 22
- "Facing the Tax Problem", published by the Twentieth Century Fund, p. 310 ..... 36
- "General Sales Taxation", by Professor Alfred D. Buehler, p. 249 ..... 35
- "General Sales or Turnover Taxation", by The National Industrial Conference Board, p. 54 ..... 36
- "The Shifting and Effects of the Federal Corporation Income Tax", by the National Industrial Conference Board, p. 157 ..... 36
- "The Shifting and Incidence of Taxation", by Professor Edwin R. A. Seligman, p. 356 ..... 34, 35

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THE DRAVO CONTRACTING COMPANY.

## REPLY BRIEF FOR APPELLEE ON REARGUMENT.

## SUMMARY OF ARGUMENT.

### I.

If a restatement of the doctrine of intergovernmental tax immunity is to be made, it should not base the validity of a tax solely on whether or not it is discriminatory, as the Attorney General suggests, but, also, on whether or not the tax palpably and directly burdens the performance of governmental functions.

### A.

While the Attorney General does not categorically answer the question propounded by this Court as to "whether the State tax imposes a burden upon the Gov-

ernment", he does not deny that the tax imposes such a burden and the effect of his argument is to admit that it does.

The Attorney General's proposition is that it is immaterial whether or not the tax in this case is a burden on the Government, provided it does not discriminate against it.

It is admitted that the affirmance of this proposition would require the overruling of three decisions of this Court; but, as we contend, it would require the overruling of fundamental principles, established by a long line of decisions, under which our dual system of government has been built up. This does not apply to net income taxes and other taxes whose effect is remote. The validation of State gross receipts taxes and sales taxes assessed against Government contracts would impose a heavy and direct burden on the Government. The actual enforcement of such taxes would directly interfere with the performance of governmental functions. A retroactive gross receipts tax would seriously impede the carrying on of governmental projects.

B.

The distinction between taxes which impose a direct burden and those whose effect is remote and incidental has been distinctly drawn by a long line of decisions of this Court.

The distinction is reasonable and practical. That such taxes are in the long run shifted to the consumer, is a proposition recognized by eminent students of the subject.

C.

The States have no power, by taxation or otherwise, to burden or impede the operation of Constitutional laws enacted by Congress to carry into execution the powers

vested in the general government. To set up discrimination as the sole test of the validity of State taxes which impose a burden on Government contracts would overthrow fundamental principles long established by this Court.

The exercise of a constitutional power by the United States is beyond the jurisdiction of State taxation. The invalidation of gross receipts taxes assessed against Government contracts works no injustice on the States. The State in which a Government project is performed is the preferred beneficiary of the project.

The proposition of the Attorney General to let down the bars against State and Federal taxes burdening the performance of governmental functions, provided such taxes be non-discriminatory, would bring about undesirable competition between State Governments and the National Government in taxing the operations of each other.

II.

The United States had exclusive jurisdiction over the river banks and the river beds on which the locks and dams were constructed.

A.

The Attorney General agrees that the United States had exclusive jurisdiction over the land acquired by it on the river banks. It is conceded that this land was acquired with the consent of West Virginia and that Congress has exclusive legislative jurisdiction thereover under Article I, Section 8, Clause 17 of the Constitution of the United States.

The United States also had exclusive jurisdiction over the parts of the river beds on which portions of the locks and dams were constructed.

The United States has the right to appropriate and occupy the beds of navigable rivers for the purpose of improving navigation by the construction of locks and dams. When the United States rightfully occupied the bed of the river, it purchased that "place" under the proper interpretation of Clause 17, it having been decided that the word "purchase" was used in said clause in its proper technical meaning and included any form of acquisition other than by descent. The West Virginia Statute specifically gives the consent of the State to the acquisition by the United States of sites for locks and dams. As such sites must necessarily include the beds of rivers and as the State has title to such beds, the consent statute manifestly contemplated the acquisition of such sites in the manner they were acquired in the case at bar. The United States, therefore, acquired exclusive legislative jurisdiction over the bed of the river where portions of the locks and dams were constructed. To hold otherwise would lead to an unsatisfactory and almost impossible demarcation of the line delimiting the jurisdiction of the United States.

III.

The tax in suit is assessed upon the entire gross income of a foreign corporation from business conducted partly in the taxing state and partly outside the taxing state and partly in interstate commerce. The assessment, therefore, violates the due process clause and the interstate commerce clause of the Constitution.

This position was taken in the Court below and at the original argument in this Court.

A large amount of the taxed receipts constitute payments made by the United States in Pennsylvania on machinery and equipment fabricated there, the title to which passed to the United States, on the making of such payments, under the terms of the contract. A large

part of the taxed receipts consisted of payments for transportaton of machinery to be installed in the locks and dams and for transportation of river craft and building equipment from Pennsylvania down the Ohio and up the Kanawha Rivers.

The receipts from extra-state transactions, interstate transactions, and local transactions were lumped together in the assessment of the tax. No apportionment was attempted by the Tax Commissioner. The statute makes no provision for such apportionment. The receipts from the four contracts in suit are not in themselves susceptible of such apportionment. Under the decisions of this Court, therefore, the entire tax must fall.

## ARGUMENT.

### QUESTIONS PROPOUNDED.

The Attorney General was requested by this Court to present his views on two questions, namely—

(1) as to the jurisdiction over the areas in which the work of the several contractors is being performed, and

(2) whether the state tax imposes a burden upon the Government.

— In his brief the Attorney General discusses the second question first, and so shall we.

### PRELIMINARY STATEMENT.

We find no categorical answer in the brief filed by the Attorney General as *Amicus Curiae* to the question of this Court as to whether or not the State tax imposes a burden upon the Government.

As we read the brief as a whole, it admits that the tax does impose a burden on the Government, but denies that the tax should be held invalid for that reason.

The initial subject considered is the doctrine of "intergovernmental tax immunity" (p. 12). It is said that the application of this doctrine has introduced "an extraordinarily large number of philosophic subtleties and contradictions" (p. 17). The brief then proceeds with an analysis of the decisions of this Court in which it is asserted these subtleties and contradictions appear.

The Attorney General apparently deems it appropriate and desirable, in answer to the question propounded, to discuss the advisability of a reexamination

and restatement of the doctrine of intergovernmental tax immunity.

The restatement which he advocates is that the validity or invalidity of any tax, imposed by one sovereign against those who deal with the other sovereign, be determined exclusively by the test as to whether or not it is discriminatory (p. 3). He would abolish the distinction heretofore applied as to whether the tax imposed a direct and immediate burden on governmental functions or was incidental and remote in its effect.

As to the advisability of a restatement of the doctrine of intergovernmental tax immunity, we feel that it would be inappropriate and out of place for us to express an opinion, favorable or unfavorable; for, in the case at bar, there is only involved the unilateral question as to whether or not a State can impose a tax which burdens and impedes the performance of a Federal function.

If, however, a restatement of the doctrine be advisable, it can be accomplished by reaffirming two principles of governmental immunity from taxation and restricting the immunities to the limitations embodied in those principles, namely: (1) that neither the National nor a State government may impose a tax affecting the other even indirectly and remotely which discriminates against the other; and (2) neither government may impose a tax which palpably and directly burdens the performance of the governmental functions of the other (p. 22 *infra*).

The limitation of intergovernmental immunities to these canons would permit the imposition by either government of non-discriminatory taxes whose burden is incidental and remote, such as taxes on the net income of

those who deal with either government; but would prohibit taxes which impose direct burdens upon the performance of governmental functions, such as gross receipts taxes imposed on governmental contracts.

The restatement suggested by the Attorney General would not only require the overruling of three decisions of this Court, as he admits, but would require the overthrow of principles under which our dual system of government has been built up. It would open forty-eight doors to an influx of general gross receipts taxes burdening and impeding the performance of constitutional functions of the United States, while giving it, the Federal Government, the right of doubtful value to burden the performance of State functions by a general gross receipts tax, which the United States has never imposed; which, in all probability, it never will impose, and which is unsound in principle and inequitable in application.

## I.

## A.

### Does the Gross Sales and Income Tax of West Virginia Impose a Direct Burden Upon the United States in the Exercise of a Constitutional Function?

#### THE BRIEF OF THE ATTORNEY GENERAL ADMITS, IN EFFECT, THAT IT DOES.

As we have said, we find no categorical answer to this question in the Attorney General's brief. He does not deny that a gross receipts tax is a direct burden upon the business affected. He does not discuss or criticize the decisions of this Court holding that such a tax is a direct burden on the business affected.

If we have read the brief of the Attorney General aright, he actually admits,—and we rather think he in-

tends to admit,—that the tax involved in this case imposes a direct burden on the Government in the exercise of a constitutional function. It is true that these admissions are not direct and are made with a certain amount of reverse English, but the fact seems to be admitted. In saying that the tax does not impose an unconstitutional burden on the Government, there is the implied admission that a burden is imposed, but that the draftsman of the brief does not regard it as unconstitutional. The brief contains the following expressions:

> "* * * the imposition of taxes such as these will ordinarily be reflected in the amounts paid its contractor by the Federal Government, with the result that it can no longer obtain contractors' services at bargain prices." (p. 3)
>
> "The United States would, it is true, realize considerable savings in undertaking its construction projects if its contractors be given a preferred status." (p. 27)
>
> "We have indicated that a tax upon the contractor, the sole result of which is to increase the cost to the sovereign by the amount of the *normal tax burden,* presents no interference with its operations." [Italics ours] (p. 34).

Is it not perfectly clear that this is but an indirect, if somewhat evasive, way of saying that taxes of the kind involved in this case are inevitably paid by the Government? This is but another way of saying that the taxes impose a burden on the Government. The Attorney General characterizes this burden as "the normal tax burden".

In fact, the position taken throughout the brief is that it is immaterial whether or not the tax in question

imposes a burden upon the Government as long as it is non-discriminatory.

The Attorney General concedes (p. 49) that the proposition for which he contends would require the overruling of three decisions of this Court, which he admits hold that a tax of the kind involved in this suit imposes a burden upon the Federal Government and impedes the performance of a constitutional function. He, therefore, admits that the decisions of this Court establish that the tax involved in this suit burdens or impedes the Federal Government; but he asks that his views on the subject be substituted for those of this Court.

The view presented in the brief is not that the tax in question is not a burden on the Government; but that it "is in no sense a threat to the capacity of the Government to perform its functions" (p. 27). In other words, the tax is a burden on the Government, but one that it can bear and still perform its functions. If the yoke is easy and the burden light, the State should be permitted to gird the yoke on the neck of the Federal Government and cinch the pack on its back.

This proposition comes in conflict with a long line of decisions which hold that a State is without power to place a direct and immediate burden, no matter how light, by taxation or otherwise, upon the performance of a Federal Governmental function; *McCulloch v. Maryland,* 4 Wheat. 316; *Johnson v. Maryland,* 254 U. S. 51; *Weston v. Charleston,* 2 Peters 449. In the case last cited, Mr. Chief Justice Marshall, in delivering the opinion of this Court, said at page 468:

> "The right to tax the contract to any extent, when made, must operate upon the power to borrow,

before it is exercised, and have a sensible influence on the contract. The extent of this influence depends on the will of a distinct government; to any extent, however inconsiderable, it is a burden on the operations of government. It may be carried to an extent which shall arrest them entirely."

The absence of power in the State to impose even a non-discriminatory tax which is a direct and immediate burden on the performance of a governmental function is discussed at pages 37 to 44 of this brief.

**THE BURDEN ON THE UNITED STATES OF TAXES OF THE KIND INVOLVED IN SUIT WOULD BE HEAVY.**

Appendix B to the brief, at page 134, indicates that, if gross receipts taxes had been in effect in half the States, sales taxes in all the States, and gasoline taxes as at present, and had been assessed against Government contracts and sales in 1936, those transactions would have cost the Government somewhere around $13,250,000 more than they did. This statement assumes gross receipts taxes at the rate of 1% of the receipts and sales taxes at the rate of 2% of the sales. The assumption of those rates would seem to be optimistic from the standpoint of the Government. The West Virginia gross receipts tax involved in this case is at the rate of 2%.

**THE ATTORNEY GENERAL'S PROPOSITION IS THAT IT IS IMMATERIAL WHETHER OR NOT THE TAX IN THIS CASE IS A BURDEN ON THE GOVERNMENT.**

As we understand the brief of the Attorney General, he favors the abolition or disregard of all distinctions as to the kinds of tax that can be levied by a State against one who deals with the Government; provided

only that the tax be non-discriminatory as against the Government.

He takes the position that the distinctions, which have been drawn by the many decisions of this Court between a tax which is a direct, immediate, and palpable burden on the Government and a tax that affects the Government only remotely and indirectly, are conceptualistic and unreal. He says that "the application of the doctrine of intergovernmental tax immunity to private persons has introduced an extraordinarily large number of philosophic subtleties and practical contradictions into the body of constitutional law." (p. 17). He thinks that the decisions of this Court on the subject "are often conceptualistic rather than practical" (p. 22). He cites a number of cases which he feels were decided on the basis of conceptualism rather than pragmatism.

The brief states, with a caveat however, that "the attributes of sovereignty may be such as to prevent a tax from being imposed on the Government itself." "Certainly", the brief continues, "the principle of the tax immunity of the sovereign itself is too firmly established now to be reexamined" (p. 26).

What the Attorney General, therefore, proposes that this Court shall do amounts to this:

Continue the "philosophic limitation against taxing the sovereign"; but permit a tax to be imposed on one who deals with the sovereign which admittedly will be passed on to the sovereign, which will be paid by the sovereign, and which will impose a direct, immediate, and palpable burden on the exercise by the sovereign of its constitutional powers.

If there ever was a conceptualistic doctrine, this is that. It is proposed to ignore realities and stick to dogma. A direct tax on the Government is to be banned; but a tax, which has the direct and immediate effect of taxing the Government, is to be permitted.

And what is the alleged conceptualistic doctrine that is to be overthrown?—A long line of decisions of this Court which establish the principle that a tax assessed against one who deals with the Government, which imposes a direct and immediate burden on, or would be an impediment to, the operations of the Government, is invalid. These decisions are based upon the proposition that States will not be permitted to accomplish by indirection the very thing they are prohibited from doing directly. Taxes which affect the Government only remotely or incidentally may be laid. The line of demarcation between these two kinds of taxes has been drawn in a long line of decisions. Taxes on the gross receipts from a Government contract or upon sales to the Government are held to be, as they are in fact, taxes on the operations of the Government. Net income taxes, property taxes, taxes on manufacturing, limited license taxes, flat taxes on occupations,—all these may be imposed by a State though they may have some indirect or remote effect on Government contracts or purchases.

There are, of course, some border line cases. In the application of general principles there are bound to be cases which fall on one side of the line or the other. It is possible that a decision here or there should be confined to its particular facts or reexamined, but that is an insufficient reason for abolishing a correct principle which has been expounded by decisions and is supported by reason and experience.

The very doctrine for which the Attorney General contends would give rise to border line cases and fine distinctions.

He contends that only taxes assessed directly against the sovereign are invalid. Would he sustain a direct tax on the operations of the Reconstruction Finance Corporation, the Federal Housing Administration, or the Panama Railroad Company? Would he have you sustain a State tax on the operations of a corporation created by the United States to carry out a governmental function all of whose stock was owned by the United States? Would he have you adopt the conceptualistic theory that taxes on such instrumentalities are not taxes on the sovereignty? He does not say (p. 22 note 7).

This Court has already pointed out that any doctrine of general application must be subject to some refinements to attain universal justice.

**THE ENFORCEMENT OF THE TAX STATUTE IN SUIT WOULD HAVE RESULTED IN AN ACTUAL INTERFERENCE WITH THE PERFORMANCE OF A GOVERNMENTAL FUNCTION.**

The Attorney General concedes (pp. 22 and 23),

> "The states are therefore constitutionally incapable of interposing obstacles to the fulfillment of this function [improvement of navigation], and any law which by design or necessary effect interferes with the ability of the Federal Government or its contractor to perform these activities would be invalid."

He goes on to say that any non-discriminatory tax, which merely increases cost, imposes no interference.

We do not know whether the Attorney General means to distinguish between a tax which is a "burden" and one which is an "interference". It would seem that he must concede that gross receipts taxes, which he admits would "burden" the Government with some $13,500,000 a year, place a burden on the Government.

If the Attorney General seeks to draw a distinction between a tax which imposes a burden on the Government and one which interferes with or impedes its operations, he is drawing a far finer and more "conceptualistic" distinction than the distinctions he complains that this Court has drawn between taxes which impose a direct and immediate burden and those whose effect is remote and incidental. A tax which places a burden on the Government necessarily impedes the Government in the performance of the function which is taxed. A tax which exacts a tribute as the condition on which one may exercise the privilege of dealing with the Government necessarily interferes with the performance of a Governmental function.

To distinguish between a tax which is a burden on, and one which impedes or interferes with, the Government is not only metaphysical, but is one which has never been drawn by this Court since the beginning. Mr. Chief Justice Marshall, in delivering the opinion of this Court in *McCulloch v. Maryland,* 4 Wheat, 316, said, at page 436,

> "The court has bestowed on this subject its most deliberate consideration. The result is a conviction that the states have no power, by taxation or otherwise, to retard, impede, burden, or in any manner control, the operations of the constitutional laws enacted by Congress to carry into execution the powers vested in the general government."

If the existence of a burden is established, the tax must fall on account of the total lack of power of any State to burden the general Government by taxation or otherwise. This subject is treated more fully at pages 37 to 44 of this brief.

But would the levy of a gross receipts tax on a contractor with the Government actually interfere with his business with the Government?

A taxing statute is composed of two parts: the first part, which levies the tax and fixes the rate, and the second part, which carries the sanction.

By reference to the taxing statute in suit, the following may be observed:

a. The tax imposes a privilege tax upon the exercise of certain privileges (R. 26);
b. The privilege can only be exercised on the condition that the tax is paid (Sec. 10, R. 36);
c. Taxes are payable quarterly on estimated amounts of gross receipts (Sec. 4, R. 33);
d. In case of delinquence for sixty days, the exercise of the privilege may be restrained (Sec. 13, R. 37).

That is to say, in the case at bar, in case of delinquency in the payment of the tax, the appellee's privilege of doing business with the United States could have been revoked.

The statute contains other usual remedies for the non-payment of the tax.

In the case at bar it is a stipulated fact that the predecessor in office of the appellant notified the appellee

that, if the taxes and penalties in suit were not paid immediately, he would distrain on the property of the appellee to collect them. The stipulation referred to is, as follows (R. 339):

> "The defendant has further notified plaintiff of said assessment, and has also notified plaintiff that unless said amount claimed as taxes and penalties, in the amount of $135,761.51, is paid immediately, that the defendant, Fred L. Fox, would be forced to proceed in accordance with the law to collect the same and to distrain on the property of plaintiff to collect the same."

At the time of the threatened distraint some of the locks and dams had been completed, but the construction of the dam at Gallipolis was still proceeding (R. 345) and had not been completed as late as the filing of the stipulation on September 11, 1936 (R. 338). The taxes involved in this case were on gross receipts of money received by the appellee from the United States during 1933 and 1934 (R. 339).

The State Tax Commissioner did not actually make a levy on the contractor's equipment, it is true; for he was restrained from doing so by the injunction issued by the court below. If the injunction had not been issued, there is no doubt that this threat would have been carried out and that actual interference would have occurred.

The three Judges of the District Court found as a fact that (R. 409)—

> "A distraint by the defendant upon the plaintiff's property, at present used in plaintiff's work under the contracts, would stop said work or materially *interfere therewith.*" (Italics ours).

The correctness of this finding is not questioned or assigned as error (R. 420).

The question of whether or not the assessment and collection of a tax would interfere with the performance of a Governmental function must go upon the assumption that the tax is valid and its collection would not be restrained.

*A Retroactive Gross Receipts Tax Would Seriously Impede the Performance of a Federal Function.*

Take the case where a gross receipts tax is enacted, or the rate increased, by a State after the contract with the Government has been entered into. Manifestly, the contractor has not included in his bid or estimate of costs a non-existent or unascertainable tax. If the tax is heavy and the contract large, the contractor might, quite probably, be unable to pay it. This is particularly true if his margin of profit was small. This is not a fanciful supposition. It actually occurred in the case at bar. The West Virginia Gross Sales and Income Tax was increased from 3/10 of 1% to 2% after two of the contracts in suit were entered into (R. 384).

The imposition of a gross receipts tax after a contract was made could easily render it impossible for the contractor to carry out his contract.

The West Virginia statute makes the payment of the tax a condition on the right to do business. If the injunction had not been issued by the court below in this case, the extent of the interference with the performance of the contract is not known; but that there would have been interference with it is certain.

The practical enforcement of the tax, therefore, as distinguished from mere burden, actually interferes with the operations of the Government.

We, therefore, submit:

1. That the answer of the Attorney General, to the question propounded by this Court as to whether the State tax imposes a burden upon the Government, has been made in the affirmative.

2. That the validation of State taxes of the kind involved in the case at bar would place a heavy burden upon the United States in the performance of Constitutional functions.

3. That the enforcement of the tax statute in suit would have resulted in actual interference with a Government project.

**B.**

**The Distinction Between Taxes Which Impose A Direct and Immediate Burden and Those Whose Effect Is Remote and Incidental Is Firmly Established and Is Reasonable and Practical.**

We are concerned, here, with a gross receipts tax —a tax by which West Virginia proposes to exact 2¢ out of every dollar received by appellee from the United States.

It is not a tax on profits or net income, but is payable even if the undertaking results in a loss to the contractor. It is the type of tax which has hitherto been designated by this Court as a tax imposing a direct and immediate burden upon the business affected. Under existing decisions of this Court, this type of tax, when

imposed upon a contractor with the Government, is invalid because its effect is to tax the Government itself.

The Attorney General contends, however, page 44:

> "We think it evident that once we pass beyond the simple criterion of whether or not the Government itself must pay the tax, and subject itself to the tax collection machinery of the State, there can be no satisfactory distinction between the types of taxes which are sought to be imposed upon the private persons who deal with the sovereign."

The foregoing contention of the Attorney General, coupled with his request for the reexamination and overruling of the three recent decisions of this Court in which the distinction between different types of taxes, imposed on persons who deal with the sovereign, has been recognized, amounts to a suggestion that that distinction be abolished. Unless this suggestion is adopted, the Attorney General's entire argument falls.

The distinction challenged is firmly imbedded in constitutional tax law as laid down by this Court. It has been recognized and enunciated in many cases.

The distinction was clearly drawn by Mr. Justice McReynolds in delivering the opinion of this Court in the case of *Northwestern Mutual Life Insurance Co. v. Wisconsin,* 275 U. S. 136. This case involved the validity of a license fee for the transaction of insurance business in Wisconsin, measured by 3% of the gross income. It was held that this charge could not be assessed against income consisting of interest on Government bonds, this Court saying (p. 140):

> "Section 76.34 undertakes to impose a charge not measured by dividends paid, as in *Home Insur-*

*ance Co. v. New York,* 134 U. S. 594, nor by net income, as in *Flint v. Stone-Tracy Co.,* 220 U. S. 107; * * * and those cases are not controlling. The distinction between an imposition the amount of which depends upon dividends or net receipts, and one measured by gross returns is clear. *U. S. Glue Co. v. Town of Oak Creek,* * * *.

* * * * * * *

"Here the statute undertook to impose a charge of 3% upon every dollar of interest received by the company from United States bonds. So much, in any event, the state took from these very receipts. This amounts, we think, to an imposition upon the bonds themselves and goes beyond the power of the state."

In the case of *Fox Film Corp. v. Doyal,* 286 U. S. 123, the validity of a gross receipts tax of the State of Georgia, as applied to royalties from copyrights on films, was involved. In discussing the nature of the tax, Mr. Chief Justice Hughes affirmed the validity of the distinction under discussion. He said (p. 126):

"As the tax is measured by gross receipts, the case is not ruled by *Educational Films Corp. v. Ward,* 282 U. S. 379, where the tax was based upon the net income of the corporation. Appellant insists, and we think rightly, that the operation of the statute here in question, in its application to gross receipts, is to impose a direct charge upon the royalties. *Northwestern Mutual Life Ins. Co. v. Wisconsin,* 275 U. S. 136, 141. See also *Crew Levick Co. v. Pennsylvania,* 245 U. S. 292, 297; *United States Glue Co. v. Oak Creek,* 247 U. S. 321, 328, 329; *New Jersey Bell Telephone Co. v. State Board,* 280 U. S. 338, 346."

In the case of *Choctaw, Oklahoma & Gulf Railroad Co. v. Harrison,* 235 U. S. 292, this Court said at page 299 of its opinion:

> "A tax upon a merchant's, manufacturer's, or miner's gross sales is not the same thing as one on his stock treated as property. Cooley on Taxation (3rd ed.), p. 1095. The former is upon his business."

In the case of *Brush v. Commissioner of Internal Revenue,* 300 U. S. 352, Mr. Justice Roberts, in delivering his dissenting opinion, drew the distinction between different kinds of taxation which the Attorney General states cannot satisfactorily be drawn. Mr. Justice Roberts said (p. 375):

> "It seems to me that the reciprocal rights and immunities of the national and a state government may be safeguarded by the observance of two limitations upon their respective powers of taxation. These are that the exactions of the one must not discriminate against the means and instrumentalities of the other and *must not directly burden* the operations of that other. To state these canons otherwise: an exaction by either government which hits the means or instrumentalities of the other infringes the principle of immunity if it discriminates against them and in favor of private citizens *or if the burden of the tax be palpable and direct rather than hypothetic and remote.* Tested by these criteria the imposition of the challenged tax in the instant case was lawful." (Italics ours).

Mr. Justice Roberts was of the opinion that the burden of the federal net income tax as imposed upon the salary of an employee of the Bureau of Water Supply of New York was remote, impalpable, and unascertain-

able; but can there be any doubt that the burden of the gross receipts tax imposed in this case is "palpable and direct" rather than "hypothetic and remote".

In the case of *Taber v. Indian Territory Illuminating Oil Co.*, 300 U. S. 1, Mr. Chief Justice Hughes, delivering the opinion of the Supreme Court, said (p. 3):

> "Our decisions distinguish between a non-discriminatory tax upon the property of an agent of government and one which imposes a direct burden upon the exertion of governmental powers."

In the case of *Stewart Dry Goods Co. v. Lewis*, 294 U. S. 550, an excise tax on retail merchants was involved. The tax was in the form of a gross sales tax graded in accordance with the volume of business done by the taxpayer. The decision of the Supreme Court was that the operation of the statute was unjustifiably unequal, whimsical, and arbitrary. In arriving at this conclusion, Mr. Justice Roberts pointed out and affirmed the distinction between gross sales and net income taxes drawn in the case of *United States Glue Co. v. Oak Creek*, 247 U. S. 321, hereinafter quoted verbatim.

The reasons for the distinction in question are explained in interstate commerce cases. In the case of *United States Glue Co. v. Town of Oak Creek*, 247 U. S. 321, it is said (pp. 328-329):

> "The difference in effect between a tax measured by gross receipts and one measured by net income, recognized by our decisions, is manifest and substantial, and it affords a convenient and workable basis of distinction between a direct and immediate burden upon the business affected and a charge that is only indirect and incidental. A tax upon gross receipts affects each transaction in pro-

portion to its magnitude and irrespective of whether it is profitable or otherwise. Conceivably it may be sufficient to make the difference between profit and loss, or to so diminish the profit as to impede or discourage the conduct of the commerce. A tax upon the net profits has not the same deterrent effect, since it does not arise at all unless a gain is shown over and above expenses and losses, and the tax cannot be heavy unless the profits are large."

In the case of *Crew Levick Co. v. Commonwealth of Pennsylvania,* 245 U. S. 292, it was held that a state gross income tax assessed against transactions in foreign commerce imposes a direct burden thereon and for that reason is invalid. This Court said (page 297):

"It operates to lay a direct burden upon every transaction in commerce by withholding, for the use of the State, a part of every dollar received in such transactions."

The brief of the Attorney General admits the validity of the distinction between taxes whose burden is direct and immediate and those whose effect is incidental and remote when applied to transactions in interstate commerce; but denies the applicability of the distinction to transactions involving the performance of a constitutional function (page 40, footnote 17).

The substance of the Attorney General's position is this:

1. There is a distinction between gross income taxes and net income taxes.

2. The distinction is such as to render gross income taxes on interstate commerce invalid.

3. This flows from the principle that a state cannot impose an additional cost on the privilege of engaging in interstate commerce, if the burden thereof, on such commerce, is direct and immediate:

4. A gross income tax on a contractor with the Government admittedly imposes a similar additional cost upon the Government.

5. The state may, however, impose such increased cost on the Government, no matter how direct and immediate its burden may be.

The reason for the difference, it is said, is that the privilege of engaging in interstate commerce requires protection from state control and interference, while the Government, in exercising its constitutional powers, requires no protection from state control and interference which does not threaten "our dual system of government".

To state the proposition is to refute it. The reason why a state cannot "impose additional cost", to use the words of the Attorney General, on interstate commerce is the same as the reason why a state cannot impose such burden on the United States in the performance of its constitutional functions. The reason rests on the absence of power in the states to assess the tax which imposes the additional cost. In the one instance, the usurped power of the state clashes with the rights of citizens under a power conferred by the Constitution of the United States; in the other, the usurped power clashes with the direct exercise of a supreme constitutional power by the United States itself.

Furthermore, the inhibition against the imposition by a state of a direct and immediate burden on the per-

formance of a constitutional function is stricter than the inhibition against the imposition of such a burden on interstate commerce. Said Mr. Justice McReynolds, in delivering the opinion of this Court in the case of *Northwestern Mutual Life Insurance Co. v. Wisconsin,* 275 U. S. 136, 140 and 141,

> "It is important to observe that although a state statute may properly impose a charge which materially affects interstate commerce without so unreasonably burdening it as to become a regulation within the meaning of the Constitution, *no state can lay any charge* on bonds of the United States. This distinction was adverted to in *Gillespie v. Oklahoma,* 257 U. S. 501, 505, and the principle found application in *Choctaw, O. & G. R. Co. v. Harrison,* 235 U. S. 292, and *Indian Territory Illuminating Oil Co. v. Oklahoma,* 240 U. S. 522." [Italics ours]

In the case of *Gillespie v. Oklahoma,* referred to in the above quotation, Mr. Justice Holmes, in delivering the opinion of this Court, enunciated the rule as follows (page 505):

> "The criterion of interference by the states with interstate commerce is one of degree. It is well understood that a certain amount of reaction upon and interference with such commerce cannot be avoided if the states are to exist and make laws. * * * The rule as to instrumentalities of the United States on the other hand is absolute in form and at least stricter in substance."

It is of more direct importance to the people of all the States that the actual performance of a function entrusted to and imposed on the general government be unimpeded than that the constitutional rights of a particularly affected citizen be untrammeled.

If, then, it be admitted that the distinction between different types of taxes is properly drawn when the business affected is interstate commerce and if it be true that this distinction should be more strictly drawn when the business affected is the performance of a Governmental function, it would seem that the Attorney General's admission is fatal to his argument that the distinction between different types of taxes, particularly in respect of their burden, should not be applied in transactions involving the performance of a constitutional function.

Furthermore, the adoption of the suggestion that this distinction be abolished would logically lead to the overruling of all interstate commerce cases in which this distinction has been applied.

The distinction between taxes which directly burden the business and those whose effect is indirect and remote has been recognized, not only in interstate commerce cases and in the cases already referred to, but in cases on both sides of the boundary line.

In the case of *Trinityfarm Construction Co. v. Grosjean,* 291 U. S. 466, it appeared that the Construction Company had contracts with the United States for the construction of levees in Louisiana for the control of the waters of the Mississippi River. In this work the contractor purchased and used gasoline. The state sought to collect a tax of 5¢ per gallon on the gasoline so purchased. The Supreme Court sustained the validity of the tax on the ground that it was not a tax on the contract for constructing the levee, but was in the nature of *a tax imposed upon the property of the contractor.* This court said (pp. 471, 472):

"It [the tax] is not laid upon the choice of means, the making of the contracts, the contracts them-

selves, or any transaction to which the federal government is a party or in which it is immediately or directly concerned. Nor is the exaction laid or dependent upon the amounts, gross or net, received by the contractor."

In the case at bar, the tax *is* "laid upon the choice of means, * * * the contracts themselves", and upon a "transaction to which the federal government is a party or in which it is immediately or directly concerned." Furthermore, the exaction is "laid or dependent upon the amounts, gross or net, received by the contractor."

In the case of *Union Pacific Railroad Co. v. Peniston,* 18 Wall. 5, the validity of a state tax upon the property of the railroad company, an instrumentality of the Government, was in issue. This Court, in an opinion by Mr. Justice Strong, held the tax valid. In discussing the distinction between the different types of taxes and their effects upon the Government, however, Mr. Justice Strong said (page 37):

"A tax upon their operations is a direct obstruction to the exercise of Federal powers."

In fact, every decision of this Court invalidating direct taxes and validating indirect taxes upon those who deal with the Federal Government is tacitly, if not expressly, based upon the very distinction here in question.

In the case of *Panhandle Oil Company v. Mississippi,* 277 U. S. 218, the distinction between different kinds of taxes which could or could not be assessed against the sale of commodities to the Government was said to rest on the practical effect of their enforcement.

If their effect is directly to retard, impede, or burden the exercise by the United States of its constitutional functions, they must fall. This Court held in that case that the State of Mississippi could not impose a gasoline sales tax on sales of gasoline to the United States, saying through Mr. Justice Butler (at page 222):

> "The validity of the taxes claimed is to be determined by the practical effect of enforcement in respect of sales to the Government. *Wagner v. City of Covington*, 251 U. S. 95, 102. A charge at the prescribed rate is made on account of every gallon acquired by the United States. It is immaterial that the seller and not the purchaser is required to report and make payment to the State. Sale and purchase constitute a transaction by which the tax is measured and on which the burden rests. The amount of money claimed by the State rises and falls precisely as does the quantity of gasoline so secured by the Government. It depends immediately upon the number of gallons. The necessary operation of these enactments when so construed is directly to retard, impede and burden the exertion by the United States of its constitutional powers to operate the fleet and hospital. *McCulloch v. Maryland, supra*, 436; *Gillespie v. Oklahoma, supra*, 505; *Jaybird Mining Co. v. Weir*, 271 U. S. 609, 613. To use the number of gallons sold the United States as a measure of the privilege tax is in substance and legal effect to tax the sale. *Telegraph Co. v. Texas*, 105 U. S. 460. *Frick v. Pennsylvania*, 268 U. S. 473, 494. And that is to tax the United States—to exact tribute on its transactions and apply the same to the support of the State."

In the case of *Graves v. Texas Co.*, 298 U. S. 393, the Supreme Court, again speaking through Mr. Justice Butler, said (page 401):

> "The validity of the tax is to be determined by the practical effect of enforcement. To apply any other test of constitutionality would be to treat 'a prohibition which is general, as if it were confined to a particular mode of doing the forbidden thing'. *Brown v. Maryland,* 12 Wheat. 419, 444. * * *. So far as concerns the federal immunity from state taxation, a tax upon storing or withdrawal so involved cannot be distinguished from the tax on sales imposed by the Mississippi statute condemned as unconstitutional."

Referring to the *Panhandle Oil Company* case and the *Graves* case just cited, the Attorney General said (pp. 48 and 49):

> "We are unable to see any distinction between the gross receipts tax upon a contract performed for the Government and a sales tax upon goods sold to it. * * *
>
> "We, therefore, recognize that the position which we have been urging is contrary to those three decisions." [*Panhandle Oil Co.* case, *Graves* case, and *Indian Motocycle* case].

The foregoing cases are not intended as a complete list of all the decisions in which the distinction under discussion has been recognized. They do, however, serve to indicate how the distinction in question has pervaded many aspects of constitutional tax law.

THE DISTINCTION BETWEEN DIFFERENT TYPES OF TAXES IS REASONABLE AND PRACTICAL.

It would seem that it would be necessary to advance cogent reasons to justify the abandonment of a principle so firmly embedded in the many decisions of this Court; namely, the principle that a single State is without power to impose a tax which directly and immediately burdens the performance by the United States of a constitutional function. Let us examine, briefly, the reasons advanced to support the suggestion that this principle be abandoned.

To sustain his request or suggestion for the abandonment of the principle referred to, the Attorney General refers to a number of cases of this Court in which real property taxes, taxes on tangible personal property, taxes on purchases of materials, net income taxes and manufacturer's taxes imposed upon contractors with the Government, have been held valid, and argues that, inasmuch as all those taxes are reflected to a greater or less degree in the cost to the Government, the distinctions between those taxes and sales taxes and gross receipts taxes should be abolished.

Is this argument sound? Is there no valid distinction between the effect upon the Government of a gross receipts tax or sales tax upon one who furnishes it with commodities or materials on the one hand and a tax on his property or net income on the other?

In actual practice, gross receipts taxes, sales taxes or other direct taxes are, in the long run, inevitably passed on by the contractor to the Government. They are charges that the contractor must pay without deduction or discount and without possibility of effecting any saving whatever. They are charges more fixed than

the prices of materials and labor, which are subject to market fluctuation. They are proportionately equal for every competitor in the field. We deem it self-evident that they would be the last items of cost a contractor would cut in bidding on a job.

Some State gross sales tax statutes expressly require the seller to shift the tax to the purchaser (e. g.: North Carolina Emergency Revenue Act of 1937, Article V, Schedule E, § 401, Corporation Trust Company North Carolina Tax Service, Report #75, dated March 16, 1937, page 9475). Such a requirement, in effect, makes the seller the mere collector of the tax from the buyer. If the Federal Government as the purchaser should receive and pay a bill for the purchase price with the tax added as a separate item, could it be contended for a moment that the tax was not actually *paid* by the Government?

A net income tax, however, stands on an entirely different footing. It is assessed solely on the contractor's profits from his venture. If there are no profits, there is no tax. Deductions are allowed for losses in other ventures and, in cases of competitive bidding, the contractor who is operating on a nonprofit basis prevents other bidders from including this tax.

The case at bar exemplifies the principle. In the bids on two of the four contracts, no profit was figured (R. 375). We must assume that, under these circumstances, no amount would have been allowed for a net income tax.

Very brief consideration will show that real estate and tangible personal property taxes assessed against the contractor, as well as net income taxes, are practically incapable of being shifted to the consumer. The question of whether the property, real or personal, is

used exclusively in the performance of government contracts or is also used in performing other contracts controls the proportion of the tax to be allocated to each job. The amount of similar taxes to which a competitor is subject must be considered. In short, many factors enter into the determination of the portion of the tax, if any, which may be shifted.

Taxes upon materials or supplies purchased by a contractor for use on a Government contract are sustained as being an incidental and remote, if any, burden on the Government. They are not assessed against the Government contract or the proceeds thereof or the means adopted by the Government to perform a function. Such taxes ordinarily are not paid by the contractor, but by the seller who seldom knows of the intended use of the materials. Many complications would arise if it were attempted to trace the materials, upon which the tax was paid, through the contractor to the Government. Practical considerations alone would render any exemption granted next to impossible of administration.

Taxes on payrolls offer much the same problems. They, also, are not taxes on any contract to which the Government is a party. Time spent on Government work and other jobs would involve complicated questions of allocation.

In short, the types of taxes, hitherto classed as indirect and remote, have no direct or necessary connection with a Government contract. The liability of the contractor for such taxes in their entirety is not necessarily or solely attributable to such contract. They are not taxes upon a contract to which the United States is a party, but are only incidental thereto.

On the contrary, a gross receipts tax on the receipts from a Government contract is attributable solely

and entirely to said contract. The amount of the tax is directly proportioned, not only to the amount of the work performed, but also to its value. The practical effect of enforcement of the tax is to tax a Government contract.

These well-known practical differences between different types of taxes render recognition of the distinctions between them simple and practical.

Economists recognize the distinction between gross receipts taxes and sales taxes, on the one hand, and net income taxes, on the other, in respect of their being shifted to the consumer.

Professor Edwin R. A. Seligman, in his book on "The Shifting and Incidence of Taxation", arrives at the following conclusion (page 356) in respect of the shifting of gross receipts taxes:

> "If we take up first the case of competition, it is clear that there can be in the given market only one price—that equivalent to the cost of production of the dearest increment of the temporary supply. Now a tax on gross receipts necessarily increases the expenses of this dearest increment; for the producer at the margin of profitable production, whose gross receipts afford him only a bare return for his outlay, without any profits, must add the tax to his price, if he is to remain as a competitor at all. *In the end, therefore, the tax must be shifted.* The extent, however, to which the tax will be shifted at any particular time will depend on the considerations that were discussed in the case of a tax on gross product; that is, on the elasticity of the demand as compared with the elasticity of the supply." (Italics ours)

Government contracts are generally let on competitive bids. The contracts in this case were so let (R. 342).

On the other hand, the nature and incidence of a net income tax are such that it cannot be shifted.

Professor Seligman says at page 362 of his said book:

> "A general or universal tax on profits, in the sense of a uniform tax on profits, does not, strictly speaking, exist any more than a general or uniform tax on all capital. But a tax may practically affect so many classes of producers in a given community, and so many different kinds of profits more or less removed from liability to competition from foreign sources, that we are justified in setting up the conception of a general tax, in contrast with an exclusive tax, on profits. *Such a general tax on net profits can never be shifted.* If profits represent the surplus above cost of production, a general tax on this surplus cannot influence the cost of production. Price cannot be altered, and the interests of the consumer cannot be affected. It is the producer who bears the tax, both immediately and ultimately." (Italics ours)

Professor Alfred D. Buehler, of the University of Vermont, in his book, "General Sales Taxation", says at page 249:

> "A general sales tax is an added business cost which tends to be shifted to consumers, in the long run."

The National Industrial Conference Board, Inc., in a practical study of the Federal corporation net income

tax, embodied in "The Shifting and Effects of the Federal Corporation Income Tax", an entire book devoted to the subject under discussion, arrives, at the following conclusion (page 157):

> "The consideration of the nature of the tax, the theory of market prices, the statistical analysis of corporation costs and profits, and the opinions and practices of business men, all confirm the conclusion that the Federal corporation income tax [net income tax] is not shifted by manufacturing and mercantile business, except under rare circumstances."

The results of a questionnaire on this subject are discussed at page 122 of this book.

In "Facing the Tax Problem," published by the Twentieth Century Fund, substantially the same conclusion is reached (page 310).

The Report of the National Industrial Conference Board on "General Sales or Turnover Taxation" says on page 54:

> "A general sales or turnover tax would be essentially a consumption tax. It would tend to increase the price of goods purchased for consumption more or less by the amount of the tax."

The decisions of this Court, therefore, that a gross receipts tax is a direct burden and that a net income tax is a remote burden on the business affected are substantiated by the facts of actual experience. The distinction between these two kinds of taxes that have been so drawn is not conceptualistic or metaphysical, but actual and real.

We, therefore, submit that "the difference in effect between a tax measured by gross receipts and one meas-

ured by net income, recognized by our decisions, is manifest and substantial", and that this distinction "affords a convenient and workable basis of distinction between a direct and immediate burden upon the business affected and a charge that is only indirect and incidental" (*United States Glue Co. v. Town of Oak Creek, supra*). This distinction, as applied to contractors with the Government, should be reaffirmed.

## C.

**"The States Have No Power, by Taxation or Otherwise, to Retard, Impede, Burden, or in Any Manner Control, the Operations of the Constitutional Laws Enacted by Congress to Carry Into Execution the Powers Vested in the General Government."**

These words are not ours, but those of Chief Justice Marshall in delivering the opinion of this Court in *McCulloch v. Maryland*.

The position of the Attorney General, however, is that it is immaterial whether or not a tax burdens or impedes the performance of a constitutional function. He says (page 3),

> "The validity of the tax should be tested only by the presence or absence of a discrimination against those dealing with the sovereign."

### DISCRIMINATION AS SOLE TEST VIOLATES FUNDAMENTAL PRINCIPLES.

Surely the Attorney General must concede that the source of the power of the State to impose any such tax, non-discriminatory or otherwise, would be a proper inquiry.

If a State has the power to grant a privilege, it can grant the privilege on a condition. The payment of a tax would seem to be a proper condition. But, if the State did not grant the privilege and if it had no power to grant the privilege, it could not impose a condition or levy a tax on the exercise of the privilege. The power to tax the privilege would have no source.

West Virginia did not empower the United States to build locks and dams on the Kanawha or any other river. That power was granted by the people of all the states and cannot be availed of by West Virginia as a source of taxation. West Virginia did not grant to the appellee the right or privilege to deal with the United States and it cannot qualify, or tax the exercise of, that right.

The fact that a State tax is non-discriminatory or reasonable in amount will not save it, if it imposes a direct and immediate burden on the performance of a Federal Governmental function. This principle is based on the entire absence of power on the part of a State to impose such tax. It is announced in cases now referred to and many others.

In delivering the opinion of this Court in the case of *Johnson v. Maryland,* 254 U. S. 51, Mr. Justice Holmes said (pages 55 and 56):

> "With regard to taxation, no matter how reasonable, or how universal and undiscriminating, the State's inability to interfere has been regarded as established since *McCulloch v. Maryland,* 4 Wheat. 316. The decision in that case was not put upon any consideration of degree but upon the entire absence of power on the part of the States to touch, in that way at least, the instrumentalities of the

United States; 4 Wheat. 429, 430; and that is the law today."

The tax involved in the case just cited was a $3 license fee which the State of Maryland sought to impose on a motor truck driver employed by the Post Office Department and which this Court held could not be collected.

In the case of *Indian Motocycle Co. v. United States,* 283 U. S. 570, this Court, by Mr. Justice VanDevanter, said (p. 575):

> "Where the principle applies it is not affected by the amount of the particular tax or the extent of the resulting interference, but is absolute. *McCulloch v. Maryland,* 4 Wheat. 316, 430; *United States v. Baltimore & Ohio R. Co.,* 17 Wall. 322, 327; *Johnson v. Maryland,* 254 U. S. 51, 55-56; *Gillespie v. Oklahoma,* 257 U. S. 501, 505; *Crandall v. Nevada,* 6 Wall. 35, 44-46."

In the case of *Weston v. The City Council of Charleston,* 2 Peters 449, this Court said (p. 468):

> "The right to tax the contract to any extent, when made, must operate upon the power to borrow, before it is exercised, and have a sensible influence on the contract. The extent of this influence depends on the will of a distinct government, to any extent, however inconsiderable, it is a burden on the operations of government."

The case just cited involved a tax on interest on government stock, with interest paid by the taxpayer allowed as a deduction. The tax was, therefore, very similar to a gross income tax.

The point of distinction between a non-discriminatory tax and a discriminatory tax is simply this: even if a State has the power to impose a tax, it must be non-discriminatory as against the United States even if it does not impose a direct burden on the exercise of Governmental powers; but, if the tax does impose a burden on the exertion of Governmental powers, it cannot be imposed by a State, even if it is non-discriminatory. This proposition was stated thus by Mr. Chief Justice Hughes, in delivering the opinion of this Court in *Taber v. Indian Territory Illuminating Oil Company,* 300 U. S. 1, 3:

> "Our decisions distinguish between a non-discriminatory tax upon the property of an agent of government and one which imposes a direct burden upon the exertion of governmental powers."

Mr. Justice Roberts, in his dissenting opinion in the case of *Brush v. Commissioner of Internal Revenue,* 300 U. S. 352, 375, enunciates the same distinction, holding, in effect, that whether the State tax is discriminatory or non-discriminatory it cannot stand "if the burden of the tax be palpable and direct rather than hypothetic and remote."

Many other cases could be cited to the same effect.

**THE EXERCISE OF A CONSTITUTIONAL POWER BY THE UNITED STATES IS BEYOND THE JURISDICTION OF STATE TAXATION.**

In the case of *Panhandle Oil Company v. Mississippi,* 277 U. S. 218, 221, Mr. Justice Butler, in delivering the opinion of this Court, said:

> "The petitioner's right to make sales to the United States was not given by the State and does

not depend on state laws; it results from the authority of the national government under the Constitution to choose its own means and sources of supply."

In the case of *Bank of New York v. Hoffman, Mayor, Connelly, Comptroller,* etc., 7 Wall. 16, Mr. Chief Justice Chase, in delivering the opinion of the Supreme Court, said (p. 25):

> "The principle of exemption is, that the States cannot control the national government within the sphere of its constitutional powers—for there it is supreme—and cannot tax its obligations for payment of money issued for purposes within that range of powers, because such taxation necessarily implies the assertion of the right to exercise such control."

The tax involved in the case just cited was a capital stock tax imposed on banking institutions by the State of New York and assessed against certificates of indebtedness of the United States. The certificates of indebtedness were issued in payment for services and supplies. It was held that a State could not tax these obligations for the payment of money. In the case at bar, the gross receipts tax was assessed against the money actually paid for services and supplies.

The brief, *Amicus Curiae,* states

> "But the attributes of sovereignty may be such as to prevent a tax from being imposed on the Government itself" (p. 26).

It seems to us that this statement demonstrates a fundamental misconception of the reason for the absence of power in any State to impose a tax which bur-

dens or impedes the performance of a constitutional function. That absence of power does not depend on any undefined attribute of sovereignty or reciprocal immunity, as that term is used in the Government's brief. The power and duty to perform certain enumerated functions is conferred and imposed upon the Federal Government by the people of all the States and any attempt by a single State to use its power of taxation "on the means employed by the Government of the Union in pursuance of the Constitution, is in itself an abuse because it is a usurpation of a power which the people of a single State cannot give."

The powers conferred upon the general Government by the people of the United States are supreme.

The proposition which we are endeavoring to establish was so clearly set forth by Mr. Chief Justice Marshall in delivering the opinion of this Court in *McCulloch v. Maryland,* 4 Wheat. 316, that its force would be lost if we attempted to paraphrase it. For this reason and for the convenience of the Court, we quote from what was there said at pages 428 and 429:

> "The people of a state, therefore, give to their government a right of taxing themselves and their property, and as the exigencies of government cannot be limited, they prescribe no limits to the exercise of this right, resting confidently on the interest of the legislator, and on the influence of the constituent over their representative, to guard them against its abuse. But the means employed by the government of the Union have no such security, nor is the right of a state to tax them sustained by the same theory. Those means are not given by the people of a particular state, not given by the constituents of the legislature, which claim

the right to tax them, but by the people of all the states. They are given by all, for the benefit of all —and upon theory, should be subjected to that government only which belongs to all.

"It may be objected to this definition, that the power of taxation is not confined to the people and property of a state. It may be exercised upon every object brought within its jurisdiction. This is true. But to what source do we trace this right? It is obvious that it is an incident of sovereignty, and is co-extensive with that to which it is an incident. All subjects over which the sovereign power of a state extends, are objects of taxation; but those over which it does not extend, are, upon the soundest principles, exempt from taxation. This proposition may almost be pronounced self-evident.

"*The sovereignty of a state extends to everything which exists by its own authority, or is introduced by its permission; but does it extend to those means which are employed by Congress to carry into execution powers conferred on that body by the people of the United States? We think it demonstrable, that it does not.* Those powers are not given by the people of a single state. They are given by the people of the United States, to a government whose laws, made in pursuance of the constitution, are declared to be supreme. Consequently, the people of a single state cannot confer a sovereignty which will extend over them.

"If we measure the power of taxation residing in a state, by the extent of sovereignty which the people of a single state possess, and can confer on its government, we have an intelligible standard, applicable to every case to which the power may be applied. We have a principle which leaves the power of taxing the people and property of a state unim-

paired; which leaves to a state the command of all its resources, and which places beyond its reach, all those powers which are conferred by the people of the United States on the government of the Union, and *all those means which are given for the purpose of carrying those powers into execution.* We have a principle which is safe for the states, and safe for the Union. We are relieved, as we ought to be, from clashing sovereignty; from interfering powers; from a repugnancy between a right in one government to pull down, what there is an acknowledged right in another to build up; from the incompatibility of a right in one government to destroy, what there is a right in another to preserve. We are not driven to the perplexing inquiry, so unfit for the judicial department, what degree of taxation is the legitimate use, and what degree may amount to the abuse of the power. *The attempt to use it on the means employed by the government of the Union, in pursuance of the constitution, is itself an abuse, because it is the usurpation of a power which the people of a single state cannot give.*" (Italics ours)

The proposition which we advance in this case is not an extension of the principle established in *McCulloch v. Maryland.* It *is* the established principle. The proposition, however, that any non-discriminatory tax assessed by a State be held valid, even though it burden and impede the performance by the United States of a constitutional function, comes in direct conflict with the principle enunciated in the decisions referred to above.

The Attorney General frankly admits that to hold the tax involved in this case valid, as applied to gross receipts from a Government contract, would require this Court to overrule its decisions in *Panhandle Oil Co. v.*

*Mississippi*, 277 U. S. 218; *Indian Motocycle Co. v. United States*, 283 U. S. 570; *Graves v. Texas Co.*, 298 U. S. 393.

We submit that to sustain the principle contended for by the Attorney General would require this Court to ignore the provision that the "Constitution and the laws of the United States which shall be made in pursuance thereof * * * shall be the supreme law of the land."

INTERGOVERNMENTAL TAX IMMUNITY IS NOT INVOLVED.

It is only by bringing into the discussion the subject of intergovernmental tax immunity that the principle that a State cannot burden the performance of a constitutional function can be in any way beclouded. We believe that principle is too clear to be beclouded. The exemption of State governments from Federal taxation which directly and immediately burdens or impedes the performance of their functions may rest on inherent attributes of sovereignty; but the exemption of the United States from taxation by a State which directly and immediately burdens or impedes the performance of its functions rests on the Constitution of the United States. Strictly speaking, the principle is not based on the *exemption* of the Federal Government from such taxation; but on the *absence of power* of a single State to impose such a tax.

## D.

### The Invalidation of Gross Receipts Taxes Assessed Against Government Contracts Works No Injustice to the States.

The invalidation of gross receipts taxes when assessed against Government contracts causes little hardship to the States. In Appendix A, page 120, to the Attorney General's brief, it is said that six states have gross receipts taxes applicable to contractors. In these six he lists Mississippi; but the Mississippi Tax Commission, on May 21, 1934, ruled that the gross receipts tax of that State could not be assessed against the receipts from a Government contract. Gross receipts taxes on specified occupations, in lieu of all other taxes, are held to be, in effect, property taxes and are valid under the decision in *Alward v. Johnson,* 282 U. S. 509. The West Virginia statute expressly states that the gross receipts tax thereby imposed is in addition to all other taxes.

Thirty-four states have net income taxes. Those taxes would not be affected by the affirmance of the decision of the court below in the case at bar.

The invalidation of the gross receipts tax as applied to Government contracts would, therefore, affect the revenues of only five states. To make up for any loss of revenue so caused, those five states could impose upon those who dealt with the Government net income taxes, property taxes, limited license taxes, and, perhaps, other taxes, the incidence of which is indirect and remote under the decisions of this Court.

The Attorney General asserts, however, that, when the United States constructs a dam in West Virginia,

it receives the benefit and protection of that State and should pay therefor in taxes. He says (p. 25),

> "Viewed solely as one who wishes to construct a dam in the Kanawha River, the United States is receiving its full measure of the governmental benefits extended by the State of West Virginia. Without them, the dam could not have been constructed unless the United States were willing to move into the ungoverned territory and set up the full panoply of governmental powers and duties in order that the dam might be constructed."

It will be observed that, under this doctrine or theory, the Government itself should be taxed even if it erected a dam by its own employees instead of through the medium of a contract. If the proposition is correct in principle, the States should have the power to tax the construction and operation of post-offices, post-roads, the maintenance of armies and navies, and any activity the government engages in, for the proposition favors the taxation of the United States when it is engaging in a constitutional governmental activity and not merely when it is performing a proprietary function.

The brief states (pp. 25 and 26),

> "Once the dam is constructed, the United States is in a position to continue receiving the benefits of the civilized society maintained by the government of West Virginia. The citizens of the surrounding territory will be educated. They will be law abiding. The State will stand ready to offer police and fire protection. Access to the dam will be over state roads. It is evident that in the maintenance, as in the construction of the dam, the United States will derive indirect benefits from the activities of the government of West Virginia, the importance of which cannot well be over-estimated."

This statement applies to anything the United States does in any State, by contract or directly.

It seems to us a fundamental misconception of the purpose and functions of the Federal Government has crept into the brief and has moulded the attitude of its draftsman toward the question propounded by this Court.

> "We the people of the United States, in order to form a more perfect Union, establish justice, insure domestic tranquillity, provide for the common defense, promote the general welfare, and secure the blessings of liberty to ourselves and our posterity, do ordain and establish this Constitution for the United States of America."

Section 8 of the Constitution gives Congress the power to regulate commerce among the States, to establish post-offices and post-roads, to raise and support armies, to provide and maintain a navy, and to do other specified things.

It was manifest that the vast majority of these functions would have to be performed within the territorial boundaries of States. The power was given unconditionally without reservation of the right of any State to control, impede, or exact tribute for the exercise of the specified powers within its geographical boundaries. The power of the United States is not limited by State boundaries. The Federal Government does not go into a State. It is already there by the mandate of the people of all the States.

To treat the Federal Government as a private corporation for profit going into West Virginia to erect and operate dams and locks, seems to us an erroneous concept.

The United States does not operate the locks for profit. It charges no tolls to vessels that pass through them.

THE CONCEPT OF THE ATTORNEY GENERAL IS CONCEPTUALISTIC AND UNREAL.

While it is true that the exercise of constitutional governmental functions by the United States is presumably intended for the benefit of all the people thereof, it can scarcely be denied that the community, where the government project is executed, receives the lion's share of the benefits of the project. This is certainly true in the great majority of cases. The ubiquitous desire of communities for the erection of post-offices and other governmental buildings can be observed by reference to the Congressional Record. Is not the Grand Coulee Dam, with its irrigation, reclamation, and power adjuncts, particularly beneficial to the State of Washington and the people of that State? The record shows that the State of Washington had intended to carry out that project itself, but the Government was induced to do it for the State, and with its cooperation.

How about the locks and dams which the United States "wished" to construct in the Kanawha River?

Let us look at the Record (R. 285), where the history of the project is given. It is there stated,

> "Improvement desired.—A great deal of public interest has been aroused in an effort to obtain better navigation facilities in the lower Kanawha River, sponsored mainly by the Kanawha Valley Improvement Association, the membership of which contains most of those interested in the navigation of the Kanawha River. In spite of the present inadequate facilities, commerce has been growing, but

its growth has not been in proportion to the industrial growth of the valley."

At page 305 of the Record it is said,

"The Kanawha Valley has two sources of commerce, both only partly developed. The first source is coal in the ground which is of such excellent quality, of such ample quantity, and so readily accessible that it will always be a source of fuel for steam, coking, byproduct, and domestic uses. The nearness of this coal to large industrial districts and thickly populated areas will assure a reliable and increasing market. The second source of commerce is the industrial development now taking place in the valley itself."

At page 279 of the Record it appears that—

"The Kanawha River is formed by the junction of the New and Gauley Rivers, is 97 miles long, and *lies wholly within the State of West Virginia.*" (Italics ours).

Who are the preferred beneficiaries of this project? Should the people of West Virginia exact a tribute for the doing of that which they so earnestly solicited? Is it not conceptualistic to a degree to say that the United States is receiving benefits from West Virginia, in the form of fire protection (for locks and dams?), access to the dams by roads (not by the River, mark you), and law abiding citizens (who will not blow up the dams, forsooth), and to say that construction of these free locks and dams on the Kanawha is not sufficient consideration to West Virginia for those benefits?

The opinion of the three judges, who heard this case in the District Court, of the policy advocated by the At-

torney General can be gleaned from the following from their opinion (R. 413):

> "With the wisdom of a policy that would cause a state to seek to gain revenue from vast projects within its boundaries, projects that give employment to the citizens of that state, to gain revenue for the state, we are not concerned; we only have to deal with the question whether the state can so hamper legitimate activities of the United States. We do not think it can."

**THE ATTORNEY GENERAL DOES NOT PROPOSE THAT THE STATES SHALL RECEIVE MUCH, IF ANY, BENEFIT FROM GROSS RECEIPTS TAXES ON FEDERAL CONTRACTS.**

The brief of the Government goes to considerable length to justify the imposition of State taxes on the performance of Federal functions (p. 22 ff.). The argument is that the United States receives benefits in the form of police and fire protection, state roads, and law abiding citizens, which the State provides (pp. 23 and 24). It says these should not be free (p. 3). No, not even if the locks and dams *are* free!

It is admitted that taxes such as those in suit would increase the cost of Government projects.

Haying arrived by this course of reasoning at this charitable, philanthropic, and paternalistic attitude toward the States, a change of heart is manifested—that, or else a change of mind and reasoning—for it is said (p. 3),

> "Further, the cost would be offset by Federal taxes upon those who deal with the States; and none can tell *whether under future tax structures the balance will lie with the central government or with the States.*" (Italics ours).

So, perhaps, the United States will get all these eulogized benefits for nothing, after all.

**It seems to us that this statement depicts the situation. With unlimited powers of taxation by the States and the United States of each other's activities, provided such taxes be non-discriminatory, we will have a race between two sovereigns in imposing taxes on each other. The United States will impose taxes on the States to pay the taxes imposed by the States on the United States and *vice versa*.**

We, therefore, respectfully submit:

(1) The gross sales and income tax of West Virginia, as applied by the Tax Commissioner to appellee's gross receipts, imposes a direct burden upon the United States in the exercise of a constitutional function.

(2) The distinction drawn by this Court between taxes which impose a direct and immediate burden and those whose effect is remote and incidental is reasonable and practical and should be reaffirmed in its application to persons contracting with the United States.

(3) The States have no power, by taxation or otherwise, to retard, impede, burden, or in any manner control the operation of the constitutional laws enacted by Congress to carry into execution the powers vested in the general Government. The assessment of a gross receipts tax upon a contractor with the Government constitutes usurpation of such power.

(4) The invalidation of gross receipts taxes assessed against Government contracts works no injustice to the States.

## II.

## The United States Had Exclusive Jurisdiction Over the Sections of the River Banks and the River Beds on Which the Locks and Dams Were Constructed.

### A.

#### THE ATTORNEY GENERAL AGREES THAT THE UNITED STATES HAD EXCLUSIVE JURISDICTION OVER THE LAND ACQUIRED BY IT ON THE RIVER BANKS.

We have already argued in our original Brief (pages 62-69) that the United States had exclusive jurisdiction over the land on the river banks to which it acquired fee simple title with the consent of West Virginia. The Attorney General agrees with us that the United States has exclusive jurisdiction over the river bank lands and that, therefore, receipts from work done on those lands may not be taxed by West Virginia.

In order that there be exclusive jurisdiction in the United States under Art. 1, § 8, cl. 17, of the Constitution of the United States, the State must consent to the purchase of places by the United States. The West Virginia consent to such purchases is contained in the West Virginia Code, 1931, Chapter 1, Art. 1, § 3 and 4 (our original brief, page 71). The construction which we placed on the statute, namely, that it gave unqualified consent to the purchase of lands for locks and dams by the United States, was not contested by the West Virginia Tax Commissioner. Therefore we gave the matter little attention in our original Brief.

The Attorney General, in arriving at the conclusion that the statute gives unqualified consent, has dealt at some length with the question of the proper construction of the statute. The Attorney General contends that

the unqualified consent given in Paragraph 1 is not qualified by other parts of the statute, and in support of that proposition he argues that:

(1) the legislative history of the statute shows that Paragraph 3 is not meant to qualify the consent given in Paragraph 1 (Attorney General's brief, pages 59-60);

(2) Paragraph 3 is not worded in the manner of a qualification. When the Legislature wished to make a qualification in Section 4, it used express words of reservation (Attorney General's brief, pages 60-61).

(3) to construe Paragraph 3 as a qualification of Paragraph 1 might make Paragraph 1 inoperative (Attorney General's brief, pages 61-62). To the Attorney General's authorities for this proposition we add the following: *United States v. Cornell,* 2 Mason 60, at 66; *Sinks v. Reese,* 19 Ohio St. 306, and 10 Op. A. G. 34;

(4) Section 4 would be totally unnecessary if Paragraph 3 limited Paragraph 1. To give effect to Section 4, Paragraph 3 should therefore not be construed to limit Paragraph 1 (Attorney General's brief, page 60):

(5) Section 4 does not affect the consent given in Paragraph 1 (Attorney General's brief, page 62).

With all this we agree.

**THE WORDING OF THE WEST VIRGINIA CONSENT STATUTE SHOWS THAT IT CONTAINS NO QUALIFICATION TO THE CONSENT THEREIN GIVEN.**

The very wording of the West Virginia consent statute shows that Paragraph 3 is not meant to qualify Paragraph 1. As stated in the Attorney General's brief (pages 53-55), the United States may acquire jurisdiction over land owned by it in one of two ways: (1) by the purchase of land with the consent of the State wherein it is located; and (2) by cession of jurisdiction to land owned by the United States otherwise acquired by it.

Both of these methods of acquisition of jurisdiction by the United States are dealt with in Sections 3 and 4 of Article 1 of the West Virginia Code of 1931, Chapter 1. (Appellee's original brief, p. 71). Paragraph 1 of Section 3 gives the consent of West Virginia to the acquisition by the United States of land by purchase, lease, condemnation, or otherwise, without qualification. No further cession of jurisdiction is necessary. This consent, in connection with clause 17 of Section 8 of Article I of the Constitution of the United States, confers on Congress exclusive legislative jurisdiction over places purchased by the United States within the geographical boundaries of West Virginia.

The second paragraph of Section 3 authorizes counties and municipalities to purchase property and "present the same to the government of the United States free of cost" and authorizes the issuance of bonds by the state to provide funds for such purchase.

The third paragraph of Section 3 then proceeds to cede concurrent jurisdiction with West Virginia over lands "so acquired" by the United States. This cession was unnecessary in connection with the purchase of

lands by the United States from citizens of West Virginia with the consent of that State. Any further cession of jurisdiction was unnecessary and superfluous. It is submitted that the third paragraph of Section 3 ceding concurrent jurisdiction applies only to property purchased by a municipality and presented to the United States. The words "so acquired" in the third paragraph properly refer to acquisition in the manner described in the paragraph immediately preceding, namely, through presentation of the land by a municipality to the United States free of cost. The phrase in the third paragraph, "if the purposes of any grant to the United States shall cease," seems clearly to apply to a grant by a municipality for certain purposes.

The first paragraph does not refer to "a grant" or to a grant for a particular purpose.

Furthermore the provision in Paragraph 3 that upon a certain contingency the ownership of the United States in "such land" shall terminate "and the right and title thereto shall reinvest in this State," cannot properly apply to conveyances by private persons to the United States, which conveyances are provided for in the first paragraph. The words, "reinvest in this State," are not a proper description of a vesting in the State of title to lands that had been conveyed to the United States by a private person, but "reinvest in this State" is a proper description of a vesting in the State of titles to land that had been granted to the United States by a political subdivision of the State, pursuant to Paragraph 2. It is unreasonable to suppose that the West Virginia Legislature would attempt to cut short an estate which a private person might convey absolutely to the United States; and, having tried to cut short the estate, that the West Virginia Legislature would provide that title would thereupon vest in the State instead of reverting

to the grantor. Such a provision would certainly violate the "due process" clause of the 14th Amendment to the United States Constitution.

It is submitted that by its very terms Paragraph 3 is not a qualification of Paragraph 1.

It follows that the United States had exclusive jurisdiction over the river bank lands on which a substantial part of the construction work was carried on and on which large portions of the completed structures are located.

By "river bank lands" we mean those lands which the United States acquired by voluntary deed or condemnation. The greater portion of each lock is located on river bank lands, although small parts of the locks extend into the river beds. A completed lock and dam structure roughly resembles a T, with the locks forming the top cross bar. The dams proper extend from the locks to the opposite bank of the river and extend a considerable distance into that opposite bank. Thus it is accurate to state that portions of the locks and dams are on the river banks and portions are on the river beds.

## B.

### THE UNITED STATES HAD EXCLUSIVE JURISDICTION OVER THOSE PARTS OF THE RIVER BEDS ON WHICH PORTIONS OF THE LOCKS AND DAMS WERE CONSTRUCTED.

A question that has not yet received adequate consideration is this: Has the United States exclusive jurisdiction over those places on the beds of the rivers on which part of the construction of the locks and dams took place? It is our contention that the United States has exclusive jurisdiction over those places, and that

therefore West Virginia may not tax receipts from work there carried on.

In the Attorney General's brief, page 69, it is stated that the United States did not acquire exclusive jurisdiction over any part of the river beds.

We recognize that in our case, in order for the United States to have exclusive jurisdiction over these places, they must be "places purchased by the consent of the legislature of the State in which the same shall be, for the erection of * * * needful buildings." (Art. 1, § 8, cl. 17, of the United States Constitution). It is submitted that there was such a purchase of the places underlying the rivers on which portions of the locks and dams were erected and that the result was to vest exclusive jurisdiction in the United States over the places so purchased. That the locks and dams are needful buildings has been demonstrated in our original brief at pages 63-65 and in the Attorney General's brief at pages 62-66. It remains for us to demonstrate that the places underlying the rivers which serve in part as the sites for the locks and dams were (1) purchased by the United States and (2) purchased with the consent of the Legislature of West Virginia.

It can hardly be denied that the bed of a river is a place within the meaning of Art. 1, § 8, cl. 17, and this proposition is impliedly admitted in the Attorney General's brief at page 102.

(1)

*There was a purchase by the United States within the meaning of the Constitution of the sections of the river beds on which portions of the locks and dams were constructed.*

As is pointed out in the Attorney General's brief (page 66), "purchase" in its proper technical meaning includes any form of acquisition other than by descent. Such was thought by Judge Evans to be the proper meaning of "purchase" as used in clause 17 when he had the question before him in *United States v. Tucker*, 122 Fed. 518, 520. The Attorney General has cited a number of cases where the word "purchase" has been similarly construed in statutes authorizing governmental units and subdivisions to purchase property (Attorney General's brief, page 67). In the case of *Burt v. Merchants' Insurance Co.*, 106 Mass. 356, the court gave to "purchase" the meaning here contended for in construing a Massachusetts statute consenting to a "purchase" of land by the United States for a needful building. Chapman, C. J., said at page 364:

> "It is to be assumed that they (the Massachusetts Legislature) used the word 'purchase' in its legal signification."

See also the opinion of Attorney General Cushing in 7 Op. A. G. 114.

Any other interpretation of the word "purchase" in clause 17 places emphasis on the formal method of acquisition by consent when there is no apparent reason for such emphasis. On the other hand, it is submitted that the Attorney General is correct when he says in his brief (page 68):

> "It was the apparent intent of the framers of the Constitution that Congress, with the consent of the State, should be able to secure land for specified purposes and to exercise exclusive jurisdiction over that area in connection with the Federal purpose."

Assuming then that "purchase" in clause 17 means any form of acquisition other than by descent, was there a purchase by the United States of those places in the river beds on which portions of the locks and dams were constructed? It is our contention that there was such a purchase from the State of West Virginia when those places were first occupied on behalf of the United States for the purpose of constructing locks and dams. When this occupation occurred, the United States acquired the places occupied. This acquisition was pursuant to what has been characterized as a servitude in the United States in respect of navigation: *Gibson v. United States*, 166 U. S. 269, at 271-272. But, says the Attorney General, the state still has title to those places on the river beds on which portions of the locks and dams were constructed because there has been no formal transfer of title by the State to the United States (Attorney General's brief, page 69. The conclusion that the United States is without title leads to what we submit is an anomalous consequence, namely, that the State has title to parts of the locks and dams (see our original brief, page 68). From a proprietary standpoint, it can hardly be contended that, once occupied by the United States, these areas and the "needful buildings" located in part thereon are any less within the Federal dominion than would be the case if the State formally conveyed to the United States a base fee title in those places. Under such circumstances, it would seem useless to require the formality of a deed. This fundamental question of constitutional law should not be influenced by formal

notions of fee simple title and the transfer thereof. When the United States exercises its paramount right to occupy sections of river beds for the construction of locks and dams and actually occupies those sections, it acquires the places it thus rightfully occupies.

It has already been shown that acquisition is "purchase" within the meaning of clause 17.

**The appropriation by the United States of sections of the river beds under a dominant right is essentially the same as the acquisition of land by condemnation.**

At page 66 of the Attorney General's brief it is stated,

> "The property condemned is, in our view, also 'purchased' under the terms of Clause 17. In its technical application, 'purchase' includes every mode of acquisition of real estate known to the law except descent. [Citing cases]".

In acquiring property by condemnation, the body politic or body corporate ordinarily exercises its right of eminent domain by simply entering upon and occupying the property and posting a bond, in proceedings provided for in the State where the land lies, to secure just compensation for the property taken to the owner thereof. The proceedings in court are merely for the purpose of ascertaining the amount of damages or compensation to which the owner of the land is entitled. The title to the land passes to the body politic or corporate upon the appropriation of the property and the approval of the bond. The title which it acquires is ordinarily described as a base fee. The base fee title confers upon the body, exercising the right of eminent domain, the right to devote the property to the purposes for which it was authorized by law to appropriate it. That title continues

as long as it is devoted to that use. When that use is discontinued, title reverts to the original owner.

The United States acquired title to sections of the river beds for the erection of portions of the locks and dams by the exercise of its right of eminent domain. By the exercise of this right of eminent domain, dominant servitude, constitutional power—no matter how the right may be termed—the United States entered upon, occupied, and appropriated sections of the river bed for the purpose of erecting locks and dams in the exercise of a power that was conferred upon it by the people of all the States. It thereby acquired a base fee to those sections of the river bed and this title will continue in the United States as long as they are occupied and used for the purpose of improving navigation.

The only difference between this method of acquiring title and ordinary condemnation proceedings is that the United States is not required to post a bond or pay compensation to the State, for the reason that the title of the State is subject to the free, unqualified, and uncontrolled right of the United States to appropriate so much of the river bed as may be necessary for the erection of locks and dams. The title of the State has been subject to this encumbrance or servitude since the Constitution of the United States was ordained and established.

The title acquired by the United States to the portions of the river beds upon which the locks and dams were erected stands upon substantially the same basis, and just as firm a basis, as title acquired by ordinary condemnation proceedings.

We submit that the proposition now advanced is fully supported by the decision of the Circuit Court

(now District Court) of the United States for the District of New Jersey in the case of *Stockton v. Baltimore & N. Y. R. Co., et al.,* 32 Federal Reporter 9, in an opinion delivered by Mr. Justice Joseph P. Bradley, then a Circuit Court Justice. In this case it was held that the power of the United States to regulate commerce included the power to take land underlying navigable streams for the purpose of improving navigation. It was further, specifically, held that the United States could take such land without compensating the State therefor. It was said that the inhibition of the Fifth Amendment is directed against the taking of private property, not property held by the State in trust for public purposes.

An appeal from this decision to this Court was dismissed on motion of counsel for appellees, without opposition: 140 U. S. 699.

The opinion of Mr. Justice Bradley was cited with approval in the case of *Scranton v. Wheeler,* 179 U. S. 141, 159.

A further reason, if one were necessary, why the State of West Virginia is entitled to no compensation for the beds of the river appropriated by the United States, is that West Virginia, by action of its Legislature, has given its unqualified consent to the acquisition by the United States of land for sites for locks and dams (see appellee's original brief, p. 71).

The Attorney General bases his position, that the United States does not have exclusive jurisdiction over the sections of the river bed on which portions of the locks and dams were erected, solely on the premise that the United States "acquired no title" thereto (p. 69). If the premise is wrong and the United States did ac-

quire a base fee title, we presume the Attorney General would readily admit that exclusive jurisdiction followed, just as in the case of land condemned.

We submit that the United States acquired a base fee title to the beds of the river on which portions of the locks and dams were erected.

(2)

*The West Virginia consent statute gives consent to the acquisition of the sections of the river beds on which portions of the locks and dams were constructed.*

There is a second question: Has the State of West Virginia consented to this acquisition? The West Virginia Code of 1931, Chapter 1, Art. 1, § 3, reads in part as follows (our original brief, p. 71):

> "The consent of this State is hereby given to the *acquisition* by the United States, or under its authority, by purchase, lease, condemnation, or *otherwise,* of any land acquired, or to be acquired in this State by the United States, from any individual, *body politic* or corporate, for sites for lighthouses, beacons, signal stations, * * *, *locks, dams,* * * *, or any needful buildings or structures or proving grounds, or works for the improvement of the navigation of any watercourse, or work of public improvement whatever, * * *" (Italics ours).

It will thus be seen that consent is specifically given (a) to the acquisition of lands in any manner, (b) from any body politic, and (c) for sites for locks and dams.

(a) It is clear that there has been an acquisition of certain sections of the beds of the rivers. Those sections are land. (The opinion in the leading case of

*Shively v. Bowlby,* 152 U. S. 1, refers a number of times to "land" underlying navigable water.) And, furthermore, those sections of the river beds were acquired by the United States.

When the United States erects on sections of the river beds portions of huge locks and dams, permanent in their nature, and exercises exclusive control thereover by virtue of the power delegated to it by the commerce clause, there is for all practical purposes no room for the exercise of property rights in those sections of the river beds by any other party than the United States. Whatever may be the legal terminology to describe the interest which the United States has acquired in the sections of the river beds on which parts of the locks and dams were constructed, the practical situation makes it idle to suggest that the United States has not acquired those sections of the river beds.

(b) The State is a body politic and so is literally within that class from which acquisition may be made by the United States under the Act. There is a good practical reason why the Act should be literally construed in this connection. In order to give full effect to the consent to acquisition of sites for locks and dams, the State must be included within the class from whom acquisition may be made. The State is the only body from which most sites for locks and dams, in so far as the sites are on river beds, may be acquired.

(c) The acquisition in this case was of sites for locks and dams.

Since the United States has acquired parts of the beds of the rivers from a body politic, the State, for the erection of locks and dams, the acquisition has been consented to by the Legislature of the State of West Vir-

ginia. If it is admitted that there must be a presumed acceptance by the United States of exclusive jurisdiction (and we make no such admission), then there has been such an acceptance of exclusive jurisdiction over the parts of the beds of the rivers on which construction was done. As stated in the Attorney General's brief, page 70, this is a "normal case" in which "acceptance by the United States may be presumed."

At page 68 of the Attorney General's brief, it is pointed out that if condemnation is held not to be a form of "purchase," "it would * * * lead to the creation of isolated patches of State territory where the United States acquired a tract largely by voluntary sale but partially by condemnation." If the acquisition by the United States of sections of the beds of the rivers is held not to be a purchase, then the United States will have exclusive jurisdiction over places on the river banks where parts of the locks and dams are located, but not exclusive jurisdiction over the places on the river beds where other parts of the locks and dams are situated.

We therefore submit that:

1. The West Virginia legislature gave unqualified consent to the acquisition by the United States of those sections of the river beds and river banks on which were constructed the locks and dams;

2. The acquisition of these sections of the river beds and river banks was a "purchase" within the meaning of Article I, section 8, clause 17 of the Constitution of the United States, and was for the erection of needful buildings;

3. The United States consequently acquired exclusive jurisdiction over the sites for the locks and dams;

4. It necessarily follows that West Virginia was without jurisdiction to tax receipts from operations on the lands on which the locks and dams were constructed.

## III.

**The Tax Is Assessed Without Apportionment Upon the Entire Gross Income of a Foreign Corporation From Business Conducted Partly In the Taxing State and Partly Outside the Taxing State and Partly In Interstate Commerce; Such An Assessment Violates the Due Process Clause and the Interstate Commerce Clause of the Constitution.**

Appellee, The Dravo Contracting Company, not only in the Court below, but also in its original brief in this Court and at the argument, charged violation of the due process clause and of the interstate commerce clause of the Constitution (appellee's original brief, pages 38 through 61). On reargument, appellee incorporates in this brief, by reference, the entire argument there made.

Our earlier argument, briefly summarized, was:

1. That a large amount, in number and value, of the transactions which gave rise to the income assessed for taxation, was performed and in many cases paid for in part outside West Virginia or constituted interstate commerce.

2. That the tax is assessed against all receipts from such transactions commingled with receipts from local operations.

3. That the essentially extrastate and interstate character of certain operations is not lost because local construction was also involved.

4. That the tax cannot be apportioned to the receipts arising from business within West Virginia.

In view of certain questions that were asked and discussions that took place at the original argument of this case, appellee here undertakes briefly to elaborate its position upon the above points.

We again point out that the gross income tax involved was assessed, without any apportionment, by the State of West Virginia against the entire receipts of appellee, in its business of contracting, from the United States, under four contracts for the construction of locks and dams in the Kanawha River.

Appellee was a Pennsylvania corporation, engaged in the general contracting business, with its principal place of business in Pittsburgh in that State. Its only plant was located at Neville Island, in the Ohio River, in the Pittsburgh district, and included a structural steel shop, a machine shop, a pattern shop, and other machinery and equipment adapted to the fabrication of steel, including space for storage. The adjacent offices included drafting rooms, accounting departments, and other necessary adjuncts of a manufacturing business. (R. 346-347).

Appellee's undertaking under the contracts was to "furnish all labor and materials, and perform all work required" for the erection and construction of the respective locks and dams (R. 61).

Appellee's compensation under the contracts was a "sum based on designations and unit rates specified in schedule appended" to the contracts. (R. 62).

The dams were of the "roller gate" type and required very large units of fabricated steel, as well as

large and expensive machinery and equipment for the operation thereof.

The general specifications of the London contract (typical of the other three (R. 427)) describe the work, materials, and equipment as (1) a 56 by 360 foot lock complete with 2 miter gates; 2 Stoney gate valves, and necessary piping; (2) power house; (3) power house machinery for operating the roller gates; (4) electrical distribution system; (5) Five 100 by 26 foot steel roller gates, individually operated by electric hoists housed on the tops of the piers; (6) Steel service bridge of the deck-truss type 565 feet in length and equipped with a 30 ton revolving crane and a 30 ton bridge-crane unit (R. 98).

The weight of each roller gate was approximately 225 tons (R. 353) and the unit price of each was $66,000, or an aggregate of $330,000 for the five (R. 394). The unit prices of some of the other items were as follows: 2 Stoney gate valves, aggregate unit price $24,000; 4 lock gate operating machines, aggregate unit price $14,000; power house machinery, $19,000; electrical revolving locomotive crane, $25,000; electric bridge crane unit, $7,500; electric illumination and control equipment, $19,800 (R. 394).

Appellee purchased outside West Virginia all materials used in the fabrication and manufacture of roller gates, lock gates, cranes, racks and spur rims, structural steel, patterns, hoisting mechanism and equipment under each of said contracts; and at its plant at Neville Island, Pennsylvania, fabricated and manufactured the same. (R. 350).

The United States knew at the time the contracts were entered into that the fabrication and manufacture would be done at Neville Island (R. 349-350).

Partial payments were made and title to fabricated materials passed to the United States in Pennsylvania (see original brief, page 47).

The machinery, equipment, and other materials purchased and fabricated in Pennsylvania, were shipped and transported by appellee by river from Pennsylvania into West Virginia (R. 351).

Other materials and supplies purchased outside West Virginia were transported by rail and river to the respective work sites (R. 356).

Towboats and barges of appellee were used in the river transportation and other river craft, fitted out with machinery and equipment, were taken from Pennsylvania into West Virginia and returned after the work was completed (R. 356, 360).

Partial payments were made upon materials (in addition to fabricated materials) upon delivery at the work site (R. 358-359).

The course of a typical fabricated article, a roller gate, was:

1. Steel purchased outside West Virginia (R. 350);
2. Fabricated at Neville Island, Pennsylvania (R. 350);
3. Assembled, inspected, and tested there (R. 350);
4. Partial payment (R. 344);
5. Title passed to the United States (R. 68);
6. Disassembled for shipment (R. 351);
7. Stored at Neville Island (R. 351);
8. Shipped by barge to dam site (R. 351);
9. Unloaded onto and into locks and dams (R. 351);

Down to this point the transactions are entirely extrastate or interstate.

10. Placed on foundations (R. 351).

On the other hand, extensive work was done and large quantities of materials were purchased in West Virginia.

From the foregoing, it abundantly appears that the business of contracting, at least in so far as the performance of appellee's four contracts with the United States was involved, was conducted by appellee partly in Pennsylvania and partly in West Virginia, and partly in commerce between said States.

It, therefore, is manifest that the gross receipts of appellee, a foreign corporation, assessed for taxation by the State of West Virginia, without any apportionment whatsoever, were derived from appellee's business of contracting conducted partly in West Virginia, partly in Pennsylvania, and partly in interstate commerce.

In other words, a part of appellee's gross receipts, assessed for taxation by West Virginia, represents appellee's compensation for fabrication of materials in Pennsylvania, as well as for plant overhead, office overhead, storage, and other intangible costs incurred under the protection of the Commonwealth of Pennsylvania.

**INCOME TAXATION BY A STATE OF THE ENTIRE INCOME, WITHOUT APPORTIONMENT, OF A FOREIGN CORPORATION FROM A BUSINESS CONDUCTED PARTLY IN THE TAXING STATE AND PARTLY IN ANOTHER, IS INVALID.**

An assessment by a State of an income tax upon the entire income of a business conducted by a foreign corporation, partly within the taxing State and partly without, is invalid under the due process clause. This principle was enunciated by Mr. Chief Justice Hughes

in the recent case of *Hans Rees' Sons, Inc., v. North Carolina,* 283 U. S. 123. In delivering the opinion of the Court, the Chief Justice said (page 133):

> "But the fact that the corporate enterprise is a unitary one, in the sense that the ultimate gain is derived from the entire business, does not mean that for the purpose of taxation the activities which are conducted in different jurisdictions are to be regarded as 'component parts of a single unit' so that the entire net income may be taxed in one State regardless of the extent to which it may be derived from the conduct of the enterprise in another State."

It is true that the *Hans Rees* case involved the reasonableness of provisions for apportionment contained in the net income tax statute of North Carolina when applied to the particular facts of the taxpayer's situation, but, we submit, the above quoted statement was a part of the actual decision of the case.

It is also true, as indicated above, that the tax involved in that case was a net income tax. We submit, however, that the principle stated applies *a fortiori* to a gross income tax.

A tax on the property or activities of a foreign corporation located or conducted outside the taxing State violates the due process clause of the Fourteenth Amendment: *Looney v. Crane Co.,* 245 U. S. 178; *Western Union Telegraph Co. v. Kansas,* 216 U. S. 1; *The Pullman Co. v. Kansas,* 216 U. S. 56; *Hans Rees' Sons, Inc., v. North Carolina, supra.* Specifically, a gross income tax on income from property outside the State violates the due process clause: *Meyer v. Wells, Fargo & Co.,* 223 U. S. 298.

The assessment made by the Tax Commissioner of West Virginia against appellee violates the due process clause of the Fourteenth Amendment of the Constitution.

INTERSTATE COMMERCE.

Identical reasoning invalidates the unapportioned assessment involved in this case because the receipts assessed arose partly from interstate commerce.

The interstate character of the acts of appellee in transporting materials and river craft in the performance of its contracts is manifest. The receipts of appellee assessed for taxation in this case arose, therefore, partly from transactions in interstate commerce.

A gross income tax upon interstate commerce is unconstitutional: *Meyer v. Wells, Fargo & Co.,* 223 U. S. 298; *Crew Levick Co. v. Pennsylvania,* 245 U. S. 292; *Galveston, H. & S. A. Ry. Co. v. Texas,* 210 U. S. 217. A gross income tax, assessed without apportionment, upon the entire income of a foreign corporation derived from business conducted partly within the taxing state and partly in interstate commerce, is, therefore, invalid.

The assessment made by the Tax Commissioner of West Virginia against appellee violates the interstate commerce clause of the Constitution.

IMPOSSIBILITY OF APPORTIONMENT OF TAX TO INCOME FROM BUSINESS IN WEST VIRGINIA.

We discussed this question in our original brief (pages 59 through 61).

We there pointed out:

1. That the Appellant's answer expressly admits that the statute contains no provision for apportionment (R. 329, 333).

2. That the statute gives no authority to the Tax Commissioner to make apportionment or even to make regulations in respect of apportionment.

3. That apportionment by the Tax Commissioner, in the absence of statutory authority, would constitute legislation by an administrative officer.

4. That the taxed income is not susceptible of apportionment.

We desire briefly to explain our position on the point last mentioned, as follows:

In the absence of some provision in the statute for apportionment of appellee's gross receipts and in the absence of authority in the Tax Commissioner to devise and apply a formula or method for apportionment thereof, said receipts cannot be apportioned.

COSTS.

Many cost figures were included in the record. Such cost figures were not prepared or intended to be used for the purpose of apportionment. The cost figures do not purport to be complete. There was no attempt to segregate the cost figures attributable to the tax years 1933 and 1934 involved in this case from the cost figures of the various contracts incurred prior and subsequent to those years. The figures were figured up to and including November 30, 1935 (R. 373). The record contains no stipulation as to the relationship, if any, between cost and gross income.

We, therefore, submit that the cost figures in the record disclose no basis whatsoever for apportionment by the Court or for an order remanding the case to the lower court for apportionment.

We, therefore, submit:

(1) That the assessment made by the Tax Commissioner against the appellee violates the due process clause of the Constitution.

(2) That the assessment made by the Tax Commissioner against the appellee violates the interstate commerce clause of the Constitution.

(3) That, under the circumstances of this case, the tax assessed cannot be apportioned to income from business done within the State of West Virginia.

**Conclusion.**

We, therefore, respectfully submit:

First: The tax, assessed by West Virginia, against the gross receipts of the appellee from the United States under the four contracts, is a direct burden on, and impediment to, the performance by the United States of a constitutional function; and the District Court properly restrained the collection thereof.

Second: The Congress of the United States has exclusive legislative jurisdiction over the places on the banks and the beds of the rivers where the locks and dams were constructed and West Virginia was without jurisdiction to tax the receipts from operations conducted on those places.

Third: The said tax assessment is a direct burden upon extrastate and interstate business. It, therefore, violates the due process clause and the interstate commerce clause of the Constitution of the United States.

Fourth: As the tax is assessed indiscriminately upon gross receipts from extrastate and interstate business and receipts from intrastate business, the Court will not attempt to allocate the tax to intrastate business and the entire tax must fall.

Respectfully submitted,

WILLIAM S. MOORHEAD,
LAWRENCE D. BLAIR,
W. CHAPMAN REVERCOMB,
W. ELLIOTT NEFFLEN,
*Counsel for the Appellee,*
*The Dravo Contracting Company.*